

**FOUNDATIONS OF THE LAW ON INDUSTRIAL  
ORGANISATIONS IN RUSSIA AND THE FORMER  
REPUBLICS OF THE USSR - 1985-1990**

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## **Abstract**

The industrial organisations introduced into the law of the USSR from 1987, and thereafter into the law of the former republics, developed upon a foundation that was rooted in Soviet law and was constructed during the period from 1985 to mid-1990.

While this study focuses on the industrial economy, certain aspects of the agrarian economy, and in particular the early history and structure of the collective farm, are considered where appropriate.

The thesis presents an entirely new understanding both of the nature of these developments and of the significance of the law on ownership. The foundations of the law on industrial organisations are conceptualised within specific heuristic models which are elaborated in an attempt to consolidate and highlight the key steps in this history. It is argued that Soviet law did not contain a concept of the "generic owner" or a developed understanding of the ownership of a juridical person, in particular by multiple owners holding "ownership interests" of that juridical person; and that their absence critically impaired a rational and coherent structure for the foundations of the law on industrial organisations both within the Stalin economic settlement and the new economic constitution of 1990.



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## 1. INTRODUCTION AND SHORT THESIS

1. ***Methodology*** This study conceptualises the "industrial organisation" within the Soviet law on ownership and posits various models, each a point of reference to be used when charting and analysing the foundations of the law on industrial organisations developed during the *perestroika* years. These models are, by definition, abstractions based principally on distinctive structures and governance regimes. They are not an attempt to reproduce, or simply paraphrase, the detail of the relevant legislation. Summaries and discussions of the minutiae of that legislation have already been adequately treated in textbooks, commentaries and translations published both within the Soviet Union and the independent former republics, as well as abroad. While reference is made to various aspects of Soviet law, including civil law and the law of juridical persons, economic law and the system of planning and price fixing, collective farm law, foreign relations law, administrative law and labour law, this study neither provides a comprehensive guide to that legislation, nor a handbook for what was the day-to-day operation of the relevant organisations.

By contrast, the analysis and models are stylised and are aimed to be used as heuristic tools for understanding and categorising the different industrial organisations and the links to the organisations (both agricultural and industrial) that preceded, and were to succeed, them. There are therefore principles that thread the models together, evolutionary and gradual, providing them with their own "history"; principles that at the outset were based on Soviet civil law, developing to those based more on market economy principles. During the course of this study, it is hoped to derive a theory of the "enterprise" in the context of Soviet and post-Soviet law and thereby distinguish "Soviet" forms of organisation from "corporate forms".

Certain key features of each of the models are summarised in the table at the end of this Section. Relevant Sections of the thesis are referred to as applicable.

2. ***1985: Origins, State Ownership and Collective Farms*** This Chapter analyses what is called "the Stalin economic settlement". It summarises the principal aspects of collective farm law and the law on ownership (based on the forms of ownership regime) which influenced the shape of the *perestroika* era industrial organisations. Finally it develops one of the key analytical tools of this study, the "ownership interest" of a juridical person, and explains why a developed understanding of the ownership interest was superfluous in the context of the traditional Soviet juridical person classified by reference to the Stalin forms of ownership.



**3. *Model 1 - The Confirmation Enterprise: Soviet State Enterprises and Associations*** This Chapter attempts to abstract the legislative enactments on socialist industrial organisations to the level of general theory and conceives of their purpose and function in terms of a single overarching model. It argues that the Soviet state traditionally protected its interests by acting in four distinct capacities: (i) as creator-owner, (ii) as property-owner, (iii) as legal sovereign, and (iv) as economic sovereign. The leitmotif of "confirmation" for this model of the Soviet industrial organisation encompasses all four capacities of the state. The state: as legal sovereign confirmed the civil law legislation setting out the nature of these industrial organisations; as economic sovereign confirmed the state plan which set out the necessity for their creation and the nature of their operations; as economic sovereign and creator-owner confirmed the decision to create them, by order of the relevant state agency; as creator-owner drafted the contents of their charters; as property-owner confirmed the designation and allocation of property to them; upon confirmation of the charter by registration, as legal sovereign conferred juridical personality upon the organisations; and finally as economic sovereign and creator-owner would confirm, when expedient, the decision for any of them to be terminated.

**4. *The Bridge - Contract-Based Associations without Juridical Personality*** The contract for joint activity is argued to be the underlying thread that linked the industrial organisations of the *perestroika* and *post-perestroika* periods back to NEP era organisations, and back further still, to the artels of pre-revolutionary Russian law. This contract incubated the notion of a contract-based association operating within the industrial economy during the Soviet period to 1985. Moreover, it provided for the possibility of founding an association by more than one person.

**5. *Model 2 - The Contract-Based Concession Enterprise: 1987 Joint Enterprises*** The significance of the joint enterprise in the history of the foundations of the law on industrial organisations is generally overlooked because it was introduced as part of the reform of foreign relations law and not explicitly as a "new" industrial organisation operating within the domestic economy. It was however the first time since the early 1920s that the Soviet state permitted the establishment of an organisation operating within the industrial economy that was not entirely owned by the state. The state therefore lost its role as creator-owner and was forced to rely principally upon a concessionary authorisation procedure and legislative diktat to ensure that its interests were protected. The interests of the participants were governed by the constitutive contract and were expressed through a voting management regime.



The joint enterprise was very different from the existing socialist industrial organisations and the contract for joint activity as used by those organisations. It was a distinct juridical person, operating outside the planned economy as an exception to the principle of state ownership of all of the means of production, and was created by parties, both foreign and Soviet, each with possibly different agendas. As such, the form of this organisation required for the first time a legal regime that tackled separately the question of "ownership of" the juridical person (by more than one person) from the question of the nature of the right of "ownership by" that juridical person. These questions were difficult to conceptualise and regulate in a coherent manner from within the logic of the Soviet "forms of ownership regime".

**6. *Model 3 - The Participation Enterprises (1987-1990): 1987 State Enterprises, 1988 Cooperative Enterprises and 1989 Leased Enterprises*** The framework of the confirmation model was explicitly undermined in the domestic Soviet economy with the introduction of the 1987 state enterprises, 1988 cooperative enterprises and the 1989 leased enterprises. It is argued that rather than being classified as three separate forms of juridical person, all of these organisations can be understood as expressions of a single model. The participation model highlights their common structural principles.

The participation model is based on the identification of "participants" within the organisational forum. The business of these enterprise was based on the personal participation of such participants. Three pillars of the participation model are developed: incentivisation (linking economic rewards to profitability); democracy and the right of management (hence giving control over profit to the participants); and coercive law as the method by which the state protects its interests (ie through legislative diktat).

The application of the participation model in each of the three expressions undermined the coherence of the Stalin forms of ownership regime almost to breaking point. By Spring 1990 the contract based concession and participation enterprises, together with the other *perestroika* reforms, necessitated a revaluation of the fundamentals of the existing system.

**7. *Perestroika or Novostroika? - The Triumph of the Enterprise (1990 Ownership Law and 1990 Law on Enterprises)*** It is argued that 1990 saw the introduction of a new economic constitution for the post-command economy (through the adoption of the 1990 Ownership Law), and a new constitution for the industrial organisation operating within that economy (through the adoption of the 1990 Law on Enterprises). Soviet law was at a crossroads: either it could have embraced *novostroika* (a rebuilding afresh) by creating the foundations of a legal system based on the market economy and its attendant corporate structures. Alternatively, it could have adopted *perestroika* (a restructuring) by preserving the framework of the Stalin



settlement and merely adjusting certain of the "problematic" aspects without implementing any fundamental reconstruction at the level of principle. This Chapter examines the choice that was made and concludes by describing and analysing the foundations of the law on industrial organisations that was built upon its legacy.



## SUMMARY OF MODELS (CHAPTERS 2-6)

MODEL	JURIDICAL PERSON ?	CONTRACT BASED ?	IDENTITY OF OWNER/CREATOR ("OWNERSHIP OF")	CAPACITY TO OWN ("OWNERSHIP BY")	ROLE OF THE STATE	AUTONOMY FROM THE STATE	MANAGEMENT
<b>Collective Farms</b> ( <i>Chapter 2</i> )	Yes ( <i>Section 2.4.1 and 2.5</i> )	No	Uncertain if members "owned" the collective farm (probably not) ( <i>Section 2.4.2</i> )	Yes: collective farm-cooperative ownership ( <i>Section 2.4.1</i> )	<ul style="list-style-type: none"> <li>Legal sovereign</li> <li>Economic sovereign (<i>Section 2.4.1</i>)</li> </ul>	Limited: State control via: <ul style="list-style-type: none"> <li>Coercive law</li> <li>Economic planning (<i>Section 2.4.1</i>)</li> </ul>	Voting: collective farm democracy ( <i>Section 2.4.1</i> )
<b>Model 1 - The Confirmation Enterprise</b> ( <i>Chapter 3</i> )	Yes ( <i>Section 3.3</i> )	No	The State: state ownership ( <i>Section 2.3.1</i> )	No: only right of operative management ( <i>Section 3.4.2</i> )	<ul style="list-style-type: none"> <li>Creator-owner</li> <li>Property-owner</li> <li>Legal sovereign</li> <li>Economic sovereign (<i>Section 3.1</i>)</li> </ul>	Limited: State control via: <ul style="list-style-type: none"> <li>Takes decision to create and terminate the enterprise/ Drafts charter (<i>Section 3.2 and 3.4.1</i>)</li> <li>Limits right to use "its" property which remained in state ownership (<i>Section 3.4.2</i>)</li> <li>Coercive law (<i>Section 3.4.3</i>)</li> <li>Economic planning (<i>Section 3.4.3</i>)</li> </ul> Operated on the basis of khozraschet	One-man management ( <i>Section 3.4.3</i> )



MODEL	JURIDICAL PERSON ?	CONTRACT BASED ?	IDENTITY OF OWNER/CREATOR ("OWNERSHIP OF")	CAPACITY TO OWN ("OWNERSHIP BY")	ROLE OF THE STATE	AUTONOMY FROM THE STATE	MANAGEMENT
The Bridge - Contract-Based Associations without Juridical Personality (Chapter 4)	No (Probably) (Section 4.6)	Yes	Contract entered into between: <ul style="list-style-type: none"> <li>Natural persons; or between</li> <li>Juridical persons (state-controlled) (Section 4.4)</li> </ul>	No	<ul style="list-style-type: none"> <li>Legal sovereign</li> <li>Economic sovereign</li> <li>Owner of/control over contracting parties (Section 4.3 and 4.5)</li> </ul>	Limited in the content of the planned economy: <ul style="list-style-type: none"> <li>Coercive law</li> <li>Economic planning</li> <li>State ownership of industrial juridical persons (Confirmation Enterprises) (Section 4.3 and 4.5)</li> </ul>	Voting (Section 4.7)



MODEL	JURIDICAL PERSON ?	CONTRACT BASED ?	IDENTITY OF OWNER/CREATOR ("OWNERSHIP OF")	CAPACITY TO OWN ("OWNERSHIP BY")	ROLE OF THE STATE	AUTONOMY FROM THE STATE	MANAGEMENT
Model 2 - The Contract-Based Concession Enterprise ( <i>Chapter 5</i> )	Yes ( <i>Section 5.3.1</i> )	Yes	Uncertain if participants "owned" the enterprise (probably not)  Contract entered into between: <ul style="list-style-type: none"> <li>• Foreign juridical persons; and</li> <li>• Soviet juridical persons</li> </ul> ( <i>Section 5.4.2.1</i> )	Probably not ( <i>Section 5.4.2.2</i> )	<ul style="list-style-type: none"> <li>• Legal sovereign</li> <li>• Economic sovereign (Indirect)</li> <li>• Owner of/control over contracting party (<i>Section 5.1</i>)</li> </ul>	<p>Increasing autonomy from the State:</p> <ul style="list-style-type: none"> <li>• Authorisation procedure/ Mandatory legal requirements (<i>Section 5.2.1, 5.2.2 and 5.2.3</i>)</li> <li>• Control over wider economy in which it operates via economic planning (<i>Section 5.2.3</i>)</li> <li>• State ownership of soviet participant (Confirmation Enterprises) (<i>Section 5.2.4</i>)</li> </ul> <p>Operated on the basis of "full" khozraschet, non-subsidy and self-financing (<i>Section 5.3.2</i>)</p>	Voting: Board and directorate ( <i>Section 5.4.3</i> )



MODEL	JURIDICAL PERSON ?	CONTRACT BASED ?	IDENTITY OF OWNER/CREATOR ("OWNERSHIP OF")	CAPACITY TO OWN ("OWNERSHIP BY")	ROLE OF THE STATE	AUTONOMY FROM THE STATE	MANAGEMENT
Model 3 - The Participation Enterprises ( <i>Chapter 6</i> )  (i) 1987 State Enterprises ( <i>Section 6.3</i> )	Yes ( <i>Section 6.3.4.3</i> )	No	The State: state ownership ( <i>Section 6.3.4.3</i> )	No: only right of operative management ( <i>Section 6.3.4.3</i> )	<ul style="list-style-type: none"> <li>• Creator-owner</li> <li>• Property-owner</li> <li>• Legal sovereign</li> <li>• Economic sovereign (<i>Section 6.3.4</i>)</li> </ul>	<p>Increasing autonomy from the State through the separation of the "private" from the "public" with the recognition of the interest of the labour collective (the participant) as separate from that of the State.</p> <p>Operated on the basis of full khozraschet and self-financing (<i>Section 6.3.2</i>)</p>	Voting: combination of centralised management and socialist self-management ( <i>Section 6.3.3</i> )



MODEL	JURIDICAL PERSON ?	CONTRACT BASED ?	IDENTITY OF OWNER/CREATOR ("OWNERSHIP OF")	CAPACITY TO OWN ("OWNERSHIP BY")	ROLE OF THE STATE	AUTONOMY FROM THE STATE	MANAGEMENT
(ii) 1988 Cooperative Enterprises (Section 6.4)	Yes (Section 6.4.1)	No	Uncertain (Section 6.4.1)	Yes: cooperative ownership (Section 6.4.4.2)	<ul style="list-style-type: none"> <li>Legal sovereign</li> <li>Economic sovereign (Indirect) (Section 6.4.4)</li> </ul>	<p>Further autonomy as State lost its roles of creator-owner and property-owner</p> <p>Operated on the basis of self-financing and non-subsidy and, in some cases, full khozraschet (Section 6.4.2)</p>	Voting: socialist self-management and broad democracy - general meeting and board (Section 6.4.3)
(iii) 1989 Leased Enterprises (Section 6.5)	Yes (Section 6.5.2.2)	Yes	<p>Organisation of Lessees (Section 6.5.2.1 and 6.5.3.1)</p> <p>Contract with the State</p>	Possibly: collective ownership (Section 6.5.3.2)	<ul style="list-style-type: none"> <li>Legal sovereign</li> <li>Economic sovereign (Indirect)</li> <li>Contractual party (Section 6.5.2.1 and 6.5.5)</li> </ul>	<p>Even further autonomy as the relationship with the State moved into the realm of contract.</p> <p>Operated on the basis of socialist economic operations (Section 6.5.6)</p> <p>[Hinted at alternative ownership regime for confirmation enterprises on the basis of "full economic jurisdiction"]</p>	Voting: socialist self-management and broad democracy (Section 6.5.4)



## 1985: ORIGINS, STATE OWNERSHIP AND COLLECTIVE FARMS

*"In this feudal world, then, we should think always of seisin and never of ownership. The tenant was seised of the land and the lord was seised of the tenant's services, but neither of them "owned" in any sense which can be intelligibly divorced from that of seisin."*

J.H. Baker

The models presented in this study have been developed from specific legislation of the *perestroika* years taking into account the wider backdrop of Soviet law and history. The state enterprises and associations of the 1980s, explained in terms of the confirmation model,<sup>1</sup> were creatures of the Stalin industrial economy and the assumptions and ideology upon which it was based. The introduction of the contract-based concession and participation enterprises in the period to 1990 saw the Soviet regime look beyond the traditional and narrow legal principles of that economy in the search for alternative foundations. These were found in the previously distinct branches of foreign relations law, collective farm law and the law of contract.<sup>2</sup> By 1990 the logic of these "new" enterprises, coupled with the radicalisation of the *perestroika* economic reforms, necessitated a reconsideration of the fundamentals of that legislative framework almost in its entirety.<sup>3</sup>

This Chapter outlines the structure and development of Soviet civil law in order to illuminate the general background from which these models emerged. It then presents a specific understanding of the "spine" of the Soviet economy,<sup>4</sup> and outlines the principles of that economy and the law on ownership. While the models developed in this study provide broad

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<sup>1</sup> See *infra* Chapter 3.

<sup>2</sup> See *infra* Chapters 5 and 6.

<sup>3</sup> See *infra* Chapter 7.

<sup>4</sup> To borrow the term famously used by Krzhizhanovsky in his report of December 1929 where he described 1929/30 as the "spinal year" of the five year plan, and indeed the concept of the Soviet spine in this study dates to that time.



deconstructed analytical stepping stones for the writing of a "history" of the foundations of the Soviet law on industrial organisations, it shall be argued that the development and classification of those organisations most abstractly are best understood in terms of the bending, breaking, and reconstitution of this Soviet spine, and in particular the failure of Soviet law on ownership to develop a comprehensive and coherent understanding of the "nature of the ownership interest" of a juridical person.<sup>5</sup> While this thesis presents an analysis of *industrial* organisations, no understanding would be complete without taking into account the framework and influences of those organisations also present within the Soviet economy, but in the agricultural sphere.

## 2.1 Origins - The Structure of Soviet Civil Law

The categorisation of Soviet civil law into various "periods" was the subject of much debate among Soviet legal scholars. The question of categorisation was especially important for a regime that was premised upon the assumption of societal development along a linear path from one mode of production to another. As such, this issue was ideologically charged. Traditionally Soviet textbooks on "The History of State and Law in the USSR" categorised the development of Soviet law into nine periods.<sup>6</sup> With regard specifically to Soviet civil law, there were a number of attempts at periodisation based on political events, economic policy and civil law initiatives.<sup>7</sup> The following is by no means comprehensive and is intended only to provide a brief sketch of the development of substantive law and thinking in order to provide a context for the subsequent analysis of the *perestroika* era industrial organisations.

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<sup>5</sup> On the concept of an "ownership interest", see in particular *infra* Sections 2.3.1, 2.4.2, 2.5, and 7.5.

<sup>6</sup> The period of the October Revolution (1917-1918); the period of military intervention and the civil war (1918-1920); the period of the transition to peaceful work regarding the establishment of a national economy (1921-1925); the period of the struggle for socialist industrialisation of the country and the collectivisation of agriculture (1926-1934); the period of the completion of the construction of socialism and the adoption of a new Constitution (1935-1941); the period of the Great Patriotic War (1941-1945); the period of the struggle for the establishment and development of the national economy in the post-war period (1945-1953); the period of the completion of the construction of socialism (1953-1960s); and thereafter, the period of developed socialism. See, for example, the following textbooks all titled *Istoriya Gosudarstva i Prava SSSR Chast' II* (Yuridicheskoe Izdatel'stvo Ministerstva Yustitsii SSSR:1947); (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1962); (Izdatel'stvo Yuridicheskaya Literatura:1966); (Izdatel'stvo Yuridicheskaya Literatura:1981). Unsurprisingly, histories of the state and law written after the demise of the Soviet Union have departed from this periodisation of the Soviet times. See, for example, I.A.Isaev, *Istoriya Gosudarstva i Prava Rossii* (Yurist:1994), pp.259-435. Western sovietologists have tended to classify the Soviet period by reference to leaders of the Communist Party noting the periods of war communism, NEP and central planning for the years until the mid-1930s. See, for example, Geoffrey Hosking, *A History of the Soviet Union* (Fontana Press:1985). However, the debate as to periodisation was never so contentious among western sovietologists as it was among Soviet scholars.

<sup>7</sup> The best overview in English of the different schools of thought regarding the periodisation of civil and economic law is: Olimpiad S. Ioffe, *Development of Civil Law Thinking in the USSR* (Dott. A. Giuffrè Editore:1989), pp.3-129.



During the first few years after the 1917 revolution, law as a formal institution was regarded as a feature of capitalist society that would rapidly disappear and would be replaced by the conscience of the proletarian. A most extreme example of the nihilism that symbolised the years of 1917-1921, known as "war communism", was the introduction of the People's Courts where, in cases of uncertainty, judges were directed to decide the issue before them, not on the basis of positive law, but by reference to their own "revolutionary legal consciousness".<sup>8</sup> Despite this, two codes were adopted during this time: the Labour Code and the Family Code.<sup>9</sup> Both were aimed at entrenching the "victory of the proletariat" and general socialist principles in these highly political areas. During these years a Soviet socialist constitution for Russia was adopted on 10 July 1918.<sup>10</sup>

The formal decision by the state to retreat to the "commanding heights" of the economy was taken at the famous 10th Congress of the Communist Party held on 8-16th March 1921.<sup>11</sup> This was to herald the period known as the New Economic Policy (or NEP) notable from a legal point of view for the law reform initiatives.

NEP lasted until 1928/9 when state planning and collectivisation were introduced on the basis of, and legitimated by, a new theory of law, "economic law", expounded by Evgeny Pashukanis, the leading theorist of the time.<sup>12</sup> Capitalism, he argued, necessitated the presence of law which structured the regulation of commodity exchange. However, under socialism and the guidance of the Communist Party, the commodification of labour and time would give way to economic relations based upon centralised administrative orders (ie the plan) leading eventually to the "withering away of private-law aspects of the legal superstructure and, finally, the progressive dissolution of the legal superstructure itself".<sup>13</sup> In the interim, these administrative relationships would be governed by a totally separate branch of law which he labelled "economic law", in contrast to "civil law".

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<sup>8</sup> Lewis H. Siegelbaum, *Soviet State and Society between Revolutions 1918-1929* (Cambridge University Press:1992), p.15.

<sup>9</sup> *Istoriya Gosudarstva i Prava SSSR, Chast' II* (Yuridicheskoe Izdatel'stvo Ministerstva Yustitsii SSSR:1941), pp.29-32, 61-63.

<sup>10</sup> "Russia" during Soviet times was referred to as the "Russian Socialist Federal Soviet Republic" (or the RSFSR). Until 1922, Russia constituted an independent state. On the creation of the USSR, see infra n.26. See *Istoriya SSSR, Epokha Sotsializma (1917-1957)* (Gosudarstvennoe Izdatel'stvo Politicheskoi Literatury:1957), pp.140-141.

<sup>11</sup> *KPSS v Rezolyutsiyakh i Resheniyakh S'ezdov, Konferentsii i Plenumov TsK, Chast' I* (Izdatel'stvo Politicheskoi Literatury:1954), p.515.

<sup>12</sup> On the question of dating the end of NEP see, R.W.Davies, *The Soviet Economy in Turmoil, 1929-1930* (Harvard University Press:1989), p.170, n.41 therein.



By the mid 1930s, Pashukanis was ousted and executed in Stalin's purges in January 1937. Planning had become an accepted feature of the Soviet economic system and in this new environment, law was seen as a necessary tool, existing in addition to the planning network and administrative instruction. The theory that law would eventually "wither away" was therefore discredited and official ideology came to focus on the concept of "legal stability" and the endurance of a distinct "new" form of legal system based on "socialist legality". This theory of socialist legality was developed by the Andrei Vyshinsky in his book "The Law of the Soviet State" published in 1936, the same year that the Stalin Constitution was adopted. As Vyshinsky explained in his classic work: "Marxism teaches the necessities of using law as one of the means of the struggle for socialism...In the Soviet state, law is entirely and completely directed against exploitation and exploiters...Stalin teaches the strengthening of socialist legislation...".<sup>14</sup> The tension between Pashukanis and Vyshinsky, between economic law and civil law, between planning instruction and contract was ever present throughout the Soviet period.<sup>15</sup> This ultimately was a reflection of the tension at the heart of Soviet economic policy between central control, through administrative instruction, and the desire for some level of decentralised discretions, through the civil law of contract.<sup>16</sup>

The codes of the RSFSR promulgated during NEP included the 1922 RSFSR Civil Code, a new redaction of the Labour Code (1922), a Land Code (1922), a Forest Code (1923), a Civil

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<sup>13</sup> Evgeny B. Pashukanis, *Allgemeine Rechtslehre und Marxismus: Versuch einer Kritik der Juristischen Grundbegriffe* (1929, reprinted Pluto Press:1989), p.133.

<sup>14</sup> Andrei Y. Vyshinsky, *The Law of the Soviet State* (1936, reprinted The Macmillan Company:1948), pp. 50-55.

<sup>15</sup> Despite often heated debate as to the place of economic law, the legal initiatives and civil law framework, first developed during NEP, still endured right up until 1991. Academic disagreements as to the role of economic law were particularly rife during the time of the adoption of the 1961 FPCivL. For an outline of the disputes, see O.S.Ioffe, *Razvitie Tsivilisticheskoi Mysli v SSSR, Chast' 1* (Izdatel'stvo Leningradskogo Universiteta:1975), pp.39-108. The two paragraphs of article 1 of the 1961 FPCivL illustrated the compromise: the first referred to the regulation of "property relations and personal non-property relations connected therewith" and the second to "socialist property" and "the state plan of economic and social development". During the late 1980s when the adoption of a new set of Fundamental Principles of Civil Legislation was being considered, there were a number of initiatives arguing for the adoption of an economic code in its stead (see V.K.Andreev, *Obsuzhdenie Proekta Khozyaistvennogo Kodeksa SSSR, SGiP* (1985), p.949). Nevertheless the 1991 FPCivL was passed in 1991 with few concessions to the economic law movement. However, still today in the post-Soviet legal systems, the notion of economic law persists as a credible academic movement. In 1994 a two-volume treatise under the title "Economic Law" was published by Professor Martem'yanov (V.S. Martem'yanov, *Khozyaistvennoe Pravo, Tom 1 i 2* (Izdatel'stvo BEK:1994)).

<sup>16</sup> This basic dichotomy is central to a number of aspects in this study including the principle of democratic centralism (infra Section 2.2), the vacillation of policy between the enterprise and association (both conceived in conceptual terms by reference to the confirmation model (infra Chapter 3)), and the balance between personal and social interests (in particular in the governance regimes of the collective farm/cooperatives and 1987 state enterprises (infra Sections 2.4.1, 6.3.3 and 6.4.3)).



Procedure Code (1923), a Code on Marriage, the Family and Adoption (1926) and a new redaction of the Criminal Code (1926).<sup>17</sup> The NEP codes were written by jurists educated during the end of the nineteenth century; a time during which, as Wortman has argued, Russia first developed an advanced "legal consciousness".<sup>18</sup> These lawyers were influenced by the Romanist civil law tradition of their European neighbours, and with the granting of the October Manifesto, they saw the creation for the first time in Russia of a limited constitutional monarchy and the establishment of a state Duma.<sup>19</sup> The Russian legal literature of the first decade of the twentieth century represented a kind of "golden age" of legal development, shining in the new democratic liberal culture.<sup>20</sup>

Such were the jurists who were co-opted by the new Soviet state to lead the legal revolution. However, Lenin took care to remind them that their work had to be guided "not [by] the corpus iuris romani, but our revolutionary concept of law."<sup>21</sup> The 1922 RSFSR Civil Code was drafted in the space of a few months predominantly by Goikhbarg.<sup>22</sup> It was based on the draft that had been submitted to the State Duma in 1913, but never passed. There were four sections: the General Part, the Law of Things (the law on ownership and collateral), the Law of Obligations, and Inheritance Law. Chapter X, in the Section on the Law of Obligations, was devoted to "Partnerships" and was divided into five parts on: the Simple Partnership, the Full Partnership, the Partnership on Belief, the Partnership with Limited Responsibility, and the Joint Stock Society (Share Partnership). Despite the fact that with the advent of state planning many of its provisions, especially in relation to the joint-stock society and partnerships, were repealed,<sup>23</sup> the structure and approach of the subsequent 1960s civil codes were clearly indebted to the 1922 RSFSR Civil Code.

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<sup>17</sup> See, *Sobranie Kodeksov RSFSR* (Yuridicheskoe Izdatel'stvo NKYu RSFSR:1928).

<sup>18</sup> See, Richard S. Wortman, *The Development of a Russian Legal Consciousness* (The University of Chicago Press:1976).

<sup>19</sup> Lionel Kochan, *Russia in Revolution 1890-1918* (Granada:1983), p.104, 115.

<sup>20</sup> In fact, the works of Shershenevich, Pakhman and Maksimov are still read and cited today by post-Soviet legal scholars searching for their Slavic roots and identity within the pre-Soviet Romanist tradition. The principal works of Shershenevich have recently been reprinted (see, for example, G.F.Shermenevich, *Uchebnik Torgovogo Prava* (1914, reprinted SPARK:1994)).

<sup>21</sup> Quoted in W.E. Butler, *Soviet Law* (2<sup>nd</sup> ed., Butterworths:1988), p.176.

<sup>22</sup> See definition of "Civil Code RSFSR" and "Civil Code" written by S.Raevich and P.Stuchka respectively in *Entsiklopediya Gosudarstva i Prava, Tom Pervyi* (Izdatel'stvo Kommunisticheskoi Akademii:1929), pp.507-521 for a contemporary account of its adoption. See also, Vladimir Gsovski, *Soviet Civil Law: Private Rights and Their Background under the Soviet Regime, Volume One* (University of Michigan Law School:1948), pp.24-25.

<sup>23</sup> *Infra* n.320.



Although the 1922 RSFSR Civil Code contained provisions governing the operation of joint-stock societies, partnerships and commercial contracts, and even a section on private ownership, it was certainly a socialist text. Chapter 1, article 1 of the code set the tone providing that "civil rights shall be protected by law, except in those instances when they are exercised contrary to their socio-economic purpose". As such all the rights contained in the code were conditional. Where entrenched rights were exercised in a manner contrary to "their social-economic purposes", no legal protection would be afforded. The 1922 RSFSR Civil Code thereby evidenced the merger of the legal with the political within the prevailing ideology of the Soviet regime. In order to decide whether the code provided protection for a certain subject, the judiciary had to not only interpret the letter of the law, but also had to promulgate policy based on the general purpose of the law. This was confirmed by article 5 of the decree implementing the code which provided that "a broad interpretation of the Civil Code shall be permitted only in the instances when it is required for the protection of the interests of workers-peasants of the state and the working mass."<sup>24</sup>

The adoption of civil codes by the other union republics of the USSR was a product of the development of the political history of the USSR and its constitutional law. In December 1922 the Declaration and the Treaty on the Formation of the USSR was made by the First Congress of Soviets of the USSR;<sup>25</sup> and on the basis of that declaration, the creation of the USSR was formalised through the adoption by the Second Congress of Soviets of the USSR in 1924 of the first Basic Law (Constitution) of the Union of Soviet Socialist Republics.<sup>26</sup> Therefore after 1924, the RSFSR (ie Russia) became merely one of the constituent "union republics" of the USSR. Throughout the late 1920s the other union republics adopted their own constitutions on the basis of the 1924 USSR Constitution. In the area of civil law, some union republics adopted their own civil codes that were broadly "analogous" to the 1922 RSFSR Civil Code, whereas in others, the 1922 RSFSR Civil Code was adopted as being directly applicable on their territory.<sup>27</sup>

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<sup>24</sup> O Vedenii v Deistvie Grazhdanskogo Kodeksa RSFSR Prinyatogo na 4 Sessii VTsIK IX Sozyva 31 Oktyabrya 1922, *SU* (1922), no.71, item 904.

<sup>25</sup> *S'ezdi Sovetov v Dokumentakh 1917-1936 Tom III* (Yuridicheskaya Literatura:1960), pp.15-22.

<sup>26</sup> Osnovnoi Zakon (Konstitutsiya) Soyuz Sovetskikh Sotsialisticheskikh Respublik reprinted in *Istoriya Sovetskoi Konstitutsii v Dokumentakh 1917-1956* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1957), pp.458-473. On the formation of the Soviet Union, see Richard Pipes, *The Formation of the Soviet Union: Communism and Nationalism 1917-1923* (Harvard University Press:1964), pp.242-297.

<sup>27</sup> The author has consulted a number of sources with a view to ascertaining the status of the 1922 RSFSR Civil Code on the territories of the other republics prior to the adoption of the 1964 FPCivL including: O.S.Ioffe, *Sovetskoe Grazhdanskoe Pravo* (Izdatel'stvo Leningradskogo Universiteta:1958), p.37; *Sovetskoe Grazhdanskoe Pravo, Tom I* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1950), pp.81-82; supra



The creation of the USSR led to a bifurcation of sources of law: those at the federal, or "all-union" level; and those at the republic, or "union republic" level. All-union legislation was to prevail over, and determine the scope of, the more detailed union republic legislation. As part of Stalin's pursuit of the centralisation of power, article 14(f) of the Stalin Constitution removed from the competence of the union republics the right to adopt their own civil codes. This was relocated to the competence of all-union bodies. Article 14 was only amended after Stalin's death on 11 February 1957 to provide for the right of all-union bodies to adopt "Fundamental Principles" of legislation. The union republic constitutions were amended accordingly to provide for their right to adopt "codes".<sup>28</sup> The introduction of the concept of all-union Fundamental Principles meant that, in the area of civil law, the RSFSR civil code was no longer to prevail or form the basis for the legislation in the other union republics. For each branch of law (including civil law), the USSR Supreme Soviet would promulgate all-union, federal, "Fundamental Principles" and on the basis of which, each union republic would adopt its own more detailed "Code".<sup>29</sup> Thus in 1961 the "Fundamental Principles of

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n.6 (1947), p.99; D.M. Genkin, I.B. Novitskii, N.V. Rabinovich, *Istoriya Sovetskogo Grazhdanskogo Prava 1917-1947* (Yuridicheskoe Izdatel'stvo Ministerstva Yustitsii SSSR:1949), pp.38-42; I.B. Novitskii, *Istoriya Sovetskogo Grazhdanskogo Prava* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1957), pp.103-104; and Vladimir Gsovski, *Soviet Civil Law: Private Rights and Their Background under the Soviet Regime, Volume Two* (University of Michigan Law School:1949), pp.3-7 (which, together with Novitskii, draw heavily upon Bakhchisaraitsev (see below for reference)). However it was difficult to derive a clear picture of the legal position for each republic, in particular as to whether the 1922 RSFSR Civil Code was simply of direct effect in the territory of the other republics; or was brought into effect in the relevant republic by the adoption of a specific implementing law of that republic (replacing the reference to the RSFSR with the name of the relevant republic, but without further amendment); or was brought into effect by an implementing law that amended the 1922 RSFSR Civil Code in a more substantive way. For example, in the case of the Tadjik SSR, Gsovski noted that "when it became a constituent republic in 1929, [it] retained the RSFSR Civil Code" (p.5); however a Tadjik SSR Civil Code was adopted on 19 December 1929 which was substantially the same as the 1922 RSFSR Civil Code but did refer to the Tadjik SSR (in the place of the RSFSR) and included minor amendments (in particular in the "Explanatory Notes" to certain articles). (*Grazhdanskii Kodeks Tadjikskoi Sovetskoi Sotsialisticheskoi Respubliki* (Yuridicheskoe Izdatel'stvo NKYu SSSR:1939)). The author has not been able to locate a copy of the principal study on this question (Kh.E.Bakhchisaraitsev, *K Istorii Grazhdanskikh Kodeksov Sovetskikh Sotsialisticheskikh Respublik* (Gosyurizdat:1948)), however a collection of the civil codes before their re-enactment in the early 1960s included civil codes for the RSFSR (1922), Ukraine SSR (1922), Belorussian SSR (1923), Uzbek SSR (undated), Georgian SSR (1923), Azerbaidzhan SSR (1920), Tadjik SSR (1929), Armenian (1923), Turkmen (1925) (see, *Grazhdanskoe Zakonodatel'stvo SSSR i Soyuznykh Respublik* (Gosyurizdat:1957)).

<sup>28</sup> *Sovetskoe Grazhdanskoe Pravo, Tom I* (Gosyurizdat:1959), pp.40-41. See, *Konstitutsiya (Osnovnoi Zakon) SSSR, Konstitutsii (Osnovnye Zakony) Soyuznykh Sovetskikh Sotsialisticheskikh Respublik* (Izdatel'stvo Izvestiya Sovetov Deputatov Trudyashchikhsya SSSR:1972).

<sup>29</sup> The concept of "fundamental principles" may be traced to the 1918 RSFSR Constitution. Article 49 referred to the right of TsIK to adopt "general state legislation (*"obshchegosudarstvennoe zakonodatel'stvo"*) on judicial structure and procedure and civil and criminal legislation. In December 1919 the "Leading Principles (*"Rukovodyashchie Nachala"*) of Criminal Law of the RSFSR" were enacted, and on the basis of those Leading Principles, the 1922 RSFSR CrimC was adopted (A.A.Gertsenzon, Sh.S.Sringauz, N.D.Durmanov, M.M.Isaev and B.S.Utevsii, *Istoriya Sovetskogo Ugolovnoego Prava* (Yuridicheskoe Izdatel'stvo Ministerstva Yustitsii SSSR:1948), p.158). The 1924



Civil Legislation of the USSR and Union Republics" was adopted and new civil codes were adopted in each union republic during the period 1963-64.<sup>30</sup>

The main change in the structure of the new 1961 FPCivL and civil codes as compared to the old 1922 RSFSR Civil Code was that the section on the "Law of Things" was renamed the "Law on Ownership" and the provisions relating to the law of collateral were moved from the section on the "Law of Things" to the section on the "Law of Obligations". This underlined the growing importance of the institute of "ownership" in the Soviet economic and legal system.<sup>31</sup> For the purposes of this study, there was one other notable change: the chapter on partnerships (Chapter X), contained in the section of the code on the Law of Obligations, was deleted. A new article was included in the chapter on juridical persons, contained in the section of the code setting out the General Provisions. This new article seemed to provide an exhaustive list of forms of juridical person (which did not include any of the former Chapter X partnerships in that list).<sup>32</sup> This legalised the *de facto* position that the NEP era industrial organisations, rooted in the law of obligations, no longer formed part of mainstream Soviet civil law and had been replaced by socialist juridical persons characterised by their form of ownership rather than contract.<sup>33</sup>

The new codes of the various union republics were essentially the same in all but the numbering of articles, just as the pre-1960s codes had been. As Feldbrugge noted, "the texts of [the legislation of] the union republics were overwhelmingly identical. The only conclusion allowed is that model code texts were actually prepared in Moscow and that only a small degree of divergence was allowed".<sup>34</sup> Despite this, and the fact that they included almost *verbatim* the provisions of the 1961 FPCivL, the mere existence of the separate union republic

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USSR Constitution in Section 2, chapter 1, article 1(o) continued this practice by providing for the "establishment of fundamental principles (*"osnov"*)" of judicial structure and procedure, civil and criminal legislation. Therefore in 1924, the 1924 FPCrimL were adopted (Ibid, p.318). The concept of "fundamental principles of legislation" found their way into the 1936 Stalin Constitution with regard to labour law, but civil and criminal law returned to being regulated by "codes" (article 14). Following constitutional amendments in 1957, the concept of "fundamental principles of legislation" as all-union framework legislation coupled with more detailed union republic codes was established for most branches of Soviet law.

<sup>30</sup> On the relationship between the 1961 FPCivL and the civil codes generally, see S.V.Polenina, *Osnovy Grazhdanskogo Zakonodatel'stva i Grazdanskie Kodeksy* (Yuridicheskaya Literatura:1968).

<sup>31</sup> The Soviet law on ownership informs many aspects of this study, but is specifically considered *infra* Sections 2.3, 3.4.2 and 7.4.

<sup>32</sup> *Supra* p.17, and *infra* Sections 2.5 and 4.1-4.3.

<sup>33</sup> *Infra* Sections 4.2-4.3.

<sup>34</sup> F.J.M.Feldbrugge, *Russian Law:The End of the Soviet System and the Role of Law* (Martinus Nijhoff Publishers:1993), p.97.



codes was to prove remarkably important during the late 1980s. The union republic codes and law meant that there was a pre-existing legal framework through which individual republics could challenge central all-union diktats, and upon which they could develop their own "national" legislation independently from federal determinants. And when the Soviet Union did eventually vanish, its constituent union republics had a legal framework of their own in place, apart from all-union legislation, that could form the basis of a new independent legal order.

This structure of civil law (the all-union 1961 FPCivL and the union republic codes) remained in place until the eventual dissolution of the Soviet Union in 1991; and until 1985, the 1961 FPCivL and union republic codes continued in force broadly unamended. There were two attempts to codify Soviet law as a whole after the 1960s;<sup>35</sup> and within these compilations, or digests, of Soviet Law generally, there were specific parts related to civil law.

Work was started in the early 1970s on the publication of the "Systematic Collection of Prevailing Legislation" of the USSR (all-union legislation) and separate collections for each of the union republics. The "SDZ", as each collection was known, was for "internal use only"; each volume was numbered and circulated among a selected list of state agencies and institutions.<sup>36</sup> They were completed in the early 1980s and most sets included supplementary updating volumes containing new legislation. There was a SDZ for the USSR and separate SDZs for each union republic with the exceptions of Armenia, Estonia and Latvia.<sup>37</sup> Section 4 of the SDZs was devoted to civil legislation.

In the early 1980s a fresh attempt to codify the legislation of the USSR and its union republics commenced. This resulted in the "Digest of Laws". Once again, there was a "Digest of Laws" for the USSR, and separate digests for each of the union republics. Publication was in binder form (the SDZ by contrast was in book form) enabling pages to be replaced as legislation was

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<sup>35</sup> "Codify" is used here in the sense of producing "compilations" or "collections" of existing legislation.

<sup>36</sup> During Soviet times, only a microfiche version of the SDZ USSR was available outside the USSR. A resulting conference of western sovietologists, mainly lawyers, was held on the significance of the SDZ USSR. The papers were published in Richard M. Bauxbaum & Cathryn Hendley (eds.), *The Soviet Sobranie of Laws: Problems of Codification and Non-Publication* (University of California, Berkeley:1991).

<sup>37</sup> While it is unlikely that a SDZ was not compiled for Armenia, Estonia or Latvia, from research conducted at the Ministries of Justice in Belarus, Turkmenistan, Kazakhstan, Tadjikistan and Uzbekistan and other libraries within the CIS, the author has not seen any evidence of the existence of a SDZ of any of these republics. Compiled before the existence of the SDZ USSR on microfiche (ibid), Walker's book was one of the few bibliographies to acknowledge even the existence of the SDZ, and then it only referenced the SDZ for the USSR (and not any of the union republics) noting: "Full publication details not available. The collection was intended for official use only and no copies are known in the West." (W.E.Butler in G.Walker (ed.), *Official Publications of the Soviet Union and Eastern Europe 1945-1980* (Mansell Publishing Ltd:1982), pp.296-7).



amended. These digests were made available to the general public, practitioners and students. Chapter 1 of section 2 of the digests was devoted to civil law. Over time the digests came to replace the SDZs. First, they contained more recent enactments and secondly, being a loose-leaf publication, updating proved cheaper and quicker. The only way to update the SDZs was the publication of supplementary volumes, the practice of which ceased in the early 1980s.

## **2.2 The Stalin Economic Settlement, Principles of the Soviet Economy and Feudal Law**

The question of the "distinctiveness" of Soviet law has spawned many pages of debate *in academe*. Although Zweigert and Kotz asserted that "it was a truth universally acknowledged that there was such a thing as a socialist legal family",<sup>38</sup> others stressed its place within the Romanist civil law tradition, and others debated the nature of this "distinctiveness" noting "Socialist", "Russian" and "Parental" influences,<sup>39</sup> as well as its "totalitarian" nature.<sup>40</sup> While it is beyond the scope of this study to revisit and evaluate the detail of these various different views, the present Section outlines the "central principles of the administration of the Soviet economy" as generally stated in Soviet legal texts and suggests yet one more strand in the context of the debate on the nature of socialist law.

Perhaps because the Soviet experiment was an ideological one, the Soviet state was obsessed with guiding principles. As such, politics and law were rooted in principles and theory. Furthermore, principles are easy to formulate, easy to learn and easy to repeat and therefore are an important tool of a centrally governed state. General principles were found in the introductory chapters of many Soviet law textbooks, and more specific principles, in the form of a numbered list, were ubiquitous in laws, decrees, campaigns and, of course, speeches, of the Soviet period. Over time these principles became concretised, almost clichés, evidencing the creed and credentials of the speaker or author. Such principles were however more than just empty rhetoric. They informed the style of the legislation as well as its content and, it shall be argued, that they formed the basis for understanding the central spine of the Stalin

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<sup>38</sup> Konrad Zweigert and Hein Kotz, *Introduction to Comparative Law, Volume 1* (2<sup>nd</sup> ed., Clarendon Press:1992), p.296. The classic treatise making the argument for the distinctiveness of Soviet Law is John N. Hazard, *Communists and Their Law - A Search for the Common Core of the Legal Systems of the Marxian Socialist States* (The University of Chicago Press:1969). Standard texts on comparative law like Zweigert and Kotz generally treated "socialist law" or the "socialist legal family" separately from other systems (see, for example, Rene David and John E. C. Brierly, *Major Legal Systems in the World Today* (Stevens & Sons:1985), p.15).

<sup>39</sup> See Harold J. Berman, *Justice in the USSR - An Interpretation of Soviet Law* (Harvard University Press: 1966).

<sup>40</sup> Supra n.34, pp.13-30.



economic system which gave rise to the confirmation model as well as the alternative structures posed by the contract-based concession and participation models.

The central principles of the administration of the Soviet economy included: the unity of political and economic administration; the unity of state socialist ownership; planning; one-man management; economic accountability; democratic centralism; socialist legality and state discipline.<sup>41</sup> Most were, in one form or another, expressed in the Brezhnev Constitution.

***The Unity of Political and Economic Administration*** The Soviet state both determined and executed policy. It was both the planner and the operator, the supervisor and the supervised, the controller and the controlled. Only in this way could the success of the dictatorship of the proletariat be ensured. As Lenin famously noted "In bourgeois society business is carried out by the landlords and not state organs, whereas here economic activity is our common affair. It itself is an interest for us of politics."<sup>42</sup> The entire economy was thus considered as a *single* indivisible complex, run for political ends. However, total central control over the economy through law could only be carried out if the state both owned all the means of production *and* had a mechanism in place for directing the micro-economic activity of those organisations that made up the Soviet economy. This was achieved through the twin principles of state ownership and the plan.

***The Unity of State Socialist Ownership*** The basic tenets were set out in the Brezhnev Constitution which provided in article 10 that the "fundamental principles of the economic system of the USSR shall comprise socialist ownership of the means of production in the form of state (all-people's) ownership...". This principle grew out of the *de facto* expropriation and nationalisation of the former Imperial Russian economy in the early years of Soviet power. The abolition of private property in land and an extension of state ownership over the means

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<sup>41</sup> See, for example, V.V. Laptev, *Pravovoe Polozhenie Gosudarstvennykh Promyshlennykh Predpriyatii v SSSR* (Izdatel'stvo Akademii Nauk SSSR:1964) pp.4-10. These principles, however, appeared in most standard Soviet "Textbooks" "Courses" or "Monographs" of the period to *perestroika*. They were sometimes even referred to as "the Leninist Principles of Administration" despite the fact that most of them were identified as key principles after his death (see, M.S.Smirtyukov, *Sovetskii Gosudarstvennyi Apparat Upravleniya* (Izdatel'stvo Politicheskoi Literatury:1982), p.50). Soviet civil law textbooks also included various sets of principles upon which civil law specifically was based. Most were the same as the general principles of the administration of the economy or expressed with a slightly different emphasis. For example, the principle of "the unity of state socialist ownership" was expressed as the civil law principle of "strengthening the protection of socialist ownership and the socialist economic system". See, for example, *Sovetskoe Grazhdanskoe Pravo, Chast' I* (Izdatel'stvo Yuridicheskaya Literatura:1986), p.22, and *Sovetskoe Grazhdanskoe Pravo, Chast' I* (Izdatel'stvo Leningradskogo Universiteta:1982), p.14.

<sup>42</sup> 43 Lenin 330. This quote was the "cliché" that appeared in most legal textbooks of the later Soviet period when addressing this principle (for example *Khozyaistvennoe Pravo* (Izdatel'stvo Yuridicheskaya Literatura:1983), p.24).



of production were in fact directly contemplated in the 10 steps "pretty generally applicable" set out by Marx and Engels in their Communist Manifesto.<sup>43</sup> During the 1930s, the law on ownership developed into a key aspect of the Soviet legal and economic system: it gave the Soviet state a direct link to all aspects of the economy; it facilitated state control of the entire productive system; and it allowed for state allocation of the fruits of industry and agriculture.

**Planning** If the law on ownership provided the legal building bricks for the creation of the Soviet economy, the plan provided the cement. As one 1950s civil law textbook put it: "socialist planning lies at the heart of Soviet civil law. Planning instructions are the precondition for transactions governing property relations between socialist organisations as well as for transactions concluded between socialist organisations and citizens."<sup>44</sup> References to state planning in the works of Lenin can be seen as early as 1918 after the conclusion of the Treaty of Brest-Litovsk,<sup>45</sup> however it was only pursued vigorously as official state policy after 1927.<sup>46</sup> The ideology of socialist planning was based both on ethical and economic considerations: planning was considered to result in the fairest distribution of goods between members of society and further encouraged the most efficient production of goods, through scientific and optimal combining of synergies. The importance of the plan was emphasised in article 11 of the Stalin Constitution and then in article 16 of the Brezhnev Constitution which provided that "the economy of the USSR shall comprise a single national-economic complex encompassing all links of social production, distribution and exchange...administration of the economy shall be carried out on the basis of state plans for economic and social development...".

**One-Man Management** The principle of one-man management broadly required that the management of state industrial organisations was carried out by a single person. This ensured that the requirements of the plan could be carried out without procrastination or debate by a committee. In addition, it allocated responsibility for the condition of the organisation to a single person.

The origins of one-man management lay in the early years of Soviet power. During the chaos in Russia that was associated with the February Revolution and the setting up of the

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<sup>43</sup> Karl Marx and Friedrich Engels, *The Communist Manifesto* (Penguin Books:1985), p.104.

<sup>44</sup> Supra n.50 (1950), p.7.

<sup>45</sup> See, for example, 36 Lenin 228; where he directs the Academy of Sciences to form a commission to examine the possibility of creating "a plan for the reorganisation of the industry and the economic revival of Russia" including the rationalisation of the location of industry and its concentration into large trusts.

<sup>46</sup> See, Boris Brutzkus, *Economic Planning in Soviet Russia* (George Routledge & Sons, Ltd.:1935), part II; and see generally, E.H.Carr and R.W.Davies, *Foundations of a Planned Economy 1926-1929, Volume One (I) and (II)* (Macmillan:1969).



provisional government of Kerenskii, workers' collectives and workers' councils were created spontaneously and often sought to take control over the management of enterprises.<sup>47</sup> Lenin exploited this situation by encouraging the seizure of control of private enterprises by the workers under the banner of his socialist revolution.<sup>48</sup> The economic shortcomings of this form of industrial organisation soon became apparent, and nationalisation provided an opportunity to reassess this management structure. Lenin argued that workers' control of nationalised enterprises was no longer necessary because the Soviet state itself comprised a dictatorship of the proletariat and as such could be trusted with safeguarding their interests as the new owner of these organisations.

Lenin developed the idea of one-man management as early as 1918. In his "Current Tasks of Soviet Power" he wrote: "as to the significance of one-man management of dictatorship power, from the point of view of the specific tasks of the present moment it is necessary to note that all large-scale machine industry...requires an unconditional and strict *singular will*, directing the joint work of hundreds, thousands, tens of thousands of people...But how can a strict singular will be ensured? By the subordination of the wills of a thousand to the will of one."<sup>49</sup> However in 1918, despite the support of Trotsky, Lenin was unable to change the management structure of collegiality to one of subordination to a "single will". In 1918 a number of different systems of management operated side-by-side. In some instances, workers' control gave way to trade union control, and in others, previous managers were compulsorily retained in their positions but were required to run the plants in the interests of the new government.<sup>50</sup> During this time Lenin continued to argue the merits of one-man management: at the 2nd All-Russian Congress of Councils of National Economy in December 1918; at the 7<sup>th</sup> All-Russian Congress of Soviets a year later; and at the 3<sup>rd</sup> All-Russian Congress of Councils of National Economy. It was only after the victory of the Red Army in the civil war and the subsequent consolidation of Soviet power that the principle of one-man management came to be accepted. It was formally approved at the 9th Congress of the Communist Party in April 1920 when, in the midst of industrial crisis, the concept of worker's control and the principle of collegiality as elements of the management of industry were finally cast aside. From the 9th Congress to the 1980's, one-man management was a central principle of state industrial organisation and was most notably recognised in the

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<sup>47</sup> See John L.H.Keep, *The Russian Revolution, A Study in Mass Mobilization* (Wiedenfeld and Nicholson:1976), chapter 21 (The Factory Committees and "Workers' Control").

<sup>48</sup> See, O Rabochem Kontrole, *SU* (1917-1918), no.3, item 35.

<sup>49</sup> 36 Lenin 200.

<sup>50</sup> See, Silvana Malle, *The Economic Organization of War Communism 1918-1921* (Cambridge University Press:1985), chapter 3.



resolution of 5 September 1929 "On Measures to Regularise the Administration of Production and Establish One-man Management".<sup>51</sup>

*Khozraschet*<sup>52</sup> While the single manager was obliged to run the state industrial organisation in accordance with the requirements of the state plan, he also had to operate its activities on the basis of "economic accountability" (a literal translation of the Russian term of art, "*khoyaistvennyi raschet*", or "*khozraschet*" for short). Where *khozraschet* applied, a state-owned juridical person at the time of its creation was given sufficient resources for its continued operation and was removed from the state system of financing.<sup>53</sup> Thereafter, with the exception of small payments to the budget, the juridical person was expected to cover its expenses with its income and would not be (or would be less) dependent on the state for continued subsidy.<sup>54</sup>

The principle of *khozraschet* was formulated during NEP, much later than those of centralised planning and one-man management. The 10<sup>th</sup> All-Russian Conference of the Communist Party held in Moscow between 26-28 May 1921 approved the principle of "broadening of the autonomy and initiative of every large-scale enterprise in matters of disposition of financial assets and material resources" and directed Sovnarkom to draw up the appropriate decrees to further this policy.<sup>55</sup> Two decrees followed: the Basic Provisions Relating to Measures For the Revitalisation of Large-Scale Industry and the Raising and Development of Production; and On *Khozraschet*.<sup>56</sup> The former noted in article 1 a new form of industrial organisation: "enterprises organised on the principles of *khozraschet*". These two pieces of legislation set out the principles for the future operation of *khozraschet*.<sup>57</sup>

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<sup>51</sup> *Resheniya Partii i Pravitel'stva po Khozyaistvennym Voprosam, Tom 2* (Izdatel'stvo Politicheskoi Literatury:1967), p.125.

<sup>52</sup> The rationale and role of *khozraschet* is examined in more detail in the first part of Chapter 3.

<sup>53</sup> Some textbooks made the distinction between *khozraschet* as an "economic category" and as a "method of management". The economic category was used to distinguish socialist enterprises and hence suitable for *khozraschet*, from capitalist enterprises based on private property which were not (see, *Khozyaistvennoe Pravo* (Izdatel'stvo Yuridicheskaya Literatura:1977), pp.129-130).

<sup>54</sup> See, Emile Burns, *Russia's Productive System* (Victor Gollancz Ltd:1930), p.48.

<sup>55</sup> Supra n.11, p.575. On the origins of state enterprise operating on the basis of *khozraschet*, see supra n.27 (1957), pp.109-117.

<sup>56</sup> Osnovnye Polozheniya o Merakh k Vosstanovleniyu Krupnoi Promyshlennosti i Podnyatiyu i Razvitiyu Proizvodstva, *SU* (1921), no.63, item 462, and O *Khozraschete*, *SU* (1922), no.4, item 43.

<sup>57</sup> On the origin of the principle of *khozraschet* generally, see, A.V. Venediktov, *Gosudarstvennaya Sotsialisticheskaya Sobstvennost'* (Izdatel'stvo Akademii Nauk SSSR:1948), pp.443-472; and on the early decrees on trusts relating to the development of *khozraschet* and commentary generally see, *NEP i Khozraschet* (Ekonomika:1991).



*Khozraschet* appeared in most pieces of civil legislation relating to the industrial economy from the mid-1920s onwards and was enshrined in the 1961 Programme of the Communist Party which provided that "it is necessary to really strengthen *khozraschet*, to strive for a stricter economy and thrift, the reduction of waste, the lowering of cost price and the increasing of profitability of production".<sup>58</sup> Furthermore the Brezhnev Constitution, in article 16, mentioned that "*khozraschet*, profit, cost of production and other economic levers and stimuli" were to be used in carrying out the instructions of centralised management.

*Khozraschet* was subsequently used in a number of other contexts in addition to its original role.<sup>59</sup> In particular "internal *khozraschet*" was applied to the operation of subdivisions of an enterprise or association which were not necessarily juridical persons in their own right. Internal *khozraschet* was aimed at ensuring that a subdivision would have sufficient resources allocated to it to be in a position to satisfy the requirements imposed upon it through the plan.

**Democratic Centralism** The balance, tensions and ambiguities between the centralising principles (eg one-man management) and the decentralising or "democratic" principles (eg *khozraschet*) within the Soviet polity and economy were perhaps best expressed by the concept of "democratic centralism".<sup>60</sup> Democratic centralism had been used to describe the operations of the Communist Party since its early days. The 5<sup>th</sup> party conference in London in 1907 noted that the organisation of the party "shall be built on the principles of democratic centralism".<sup>61</sup> A definition was developed in article 18 of the 1934 Communist Party Statute which explained democratic centralism as "(a) the electability of all leading organs of the party from the highest to the lowest; (b) periodic accountability of party organs before their party organisations; (c) strict party discipline and subordination of the minority to the majority; and (d) the absolute binding nature of decisions of the highest organs over the lowest and upon all members of the party".<sup>62</sup> This principle eventually found expression in the Brezhnev Constitution. Article 3 of the Brezhnev Constitution described democratic centralism in the

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<sup>58</sup> *KPSS v Rezolyutsiyakh i Resheniyakh S'ezdov, Konferentsii i Plenumov TsK, Tom 8* (Izdatel'stvo Politicheskoi Literatury:1972), p.264.

<sup>59</sup> These included internal *khozraschet*, administrative *khozraschet* as well as *khozraschet* of the production system as a whole; *khozraschet* of the economic system as a whole; *khozraschet* in organs of economic administration (supra n.42, pp.124-136).

<sup>60</sup> See *Sovetskaya Sotsialisticheskaya Demokratiya* (Izdatel'stvo Nauk:1963), pp.145-156. On the seven different spheres to which the principle of democratic centralism was applied, see *Sovetskoe Administrativnoe Pravo* (Izdatel'stvo Yuridicheskaya Literatura:1973), p.33. See also, D.D. Tsabriya, *Demokratichesii Tsentralizm: Nekotorye Voprosy Teorii i Praktiki*, *SGiP* (1986), no.1, p.30.

<sup>61</sup> Supra n.11, p.170.

<sup>62</sup> *KPSS v Rezolyutsiyakh i Resheniyakh S'ezdov, Konferentsii i Plenumov TsK, Chast' III* (Gosudarstvennoe Izdatel'stvo Politicheskoi Literatury:1954), pp.235-6.



political arena as "the electability of all organs of state power from the bottom to the top, their accountability to the people and the binding nature of decisions of the superior organs on the inferior"; and in the economic area as a principle which "shall combine unified direction with initiative and creative activity at the grassroots level with the responsibility of each state organ and official for the matters to which they have been entrusted". Article 15 of the Brezhnev Constitution expanded this concept providing that "the direction of the economy shall be carried out on the basis of state plans...combining centralised management [on the one hand] with the economic independence and initiative of enterprises...*khozraschet*, profit, cost of production and other economic levers and stimuli [on the other]."

As such, the principle of democratic centralism embodied a number of the tensions within the Soviet polity and economy: between centralisation and decentralisation within the macro-economy;<sup>63</sup> and also, within the micro-economy, between administrative orders (based on the plan) and "market" mechanisms (such as profit and incentives realised through the law of contract). Democratic centralism was simply a fulcrum upon which such a balance could be struck from time to time. It was therefore an adaptable and flexible principle, and, as will be shown in this study, was applied by the Soviet regime to the very different governance regimes of the confirmation enterprises, the collective farms and the participation enterprise.

***State Discipline and Socialist Legality*** While democratic centralism balanced instruction and autonomy, the principles of discipline and legality ensured that the balancing act would not at any time threaten the perpetuation of the regime itself. Both discipline and an adherence to socialist legality had their roots in the Stalin "red terror" years of the thirties and Vyshinsky's legal doctrine.<sup>64</sup> As a 1953 legal dictionary defined the term: "Socialist legality is one of the fundamental methods for the securing of the dictatorship of the proletariat, reflected in the *unconditional and exact compliance* by all state agencies, officials and citizens with the laws and other normative acts of the socialist state".<sup>65</sup> This definition extended the requirement of "exact compliance" only to agencies, officials and citizens *of the state* but not to the state itself, which in accordance with the concept of socialist legality, defined the boundaries of "the legal" without being subject to them. Legislative enactments therefore became a tool of the state, a series of rules expressing state policy and ideology that had to be, and should be,

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<sup>63</sup> See *infra* Chapter 3.

<sup>64</sup> In general, see *Pravovye Garantii Zakonnosti v SSSR* (Izdatel'stvo Akademii Nauk SSSR:1961). For an account of the performance of Vyshinsky at the "greatest trial of all", see Robert Conquest, *The Great Terror: a Reassessment* (Hutchinson:1968), chapter 12.

<sup>65</sup> *Yuridicheskii Slovar'* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1953), p.632 [emphasis added]. As to the suppression of democratic process and fractionalism in early Soviet history, see *infra* Section 6.3.3.



obeyed and "socialist legality" expressed a crude form of absolute positivism giving rise to a legal system without any intrinsic norms or values in and of itself.<sup>66</sup>

***The Communist Party*** While the administration of the Soviet economy was embedded in the aforementioned principles, the co-ordination of that economy through law was supervised and policed by the Communist Party in all its manifestations: from the Politburo down to local factory committees.<sup>67</sup> Study of the history and role of the Communist Party was compulsory for all Soviet students,<sup>68</sup> and its organisation shadowed that of the state political administration.<sup>69</sup> The apex of the Party and the polity was the point of *de facto* merger of these two administrations: the General Secretary of the Communist Party was usually also the Chairman of the Presidium of the Supreme Soviet and as such, the Head of State. In addition to its structure, in terms of actual legislation, important decrees were sometimes adopted jointly, by the USSR Council of Ministers (ie the Soviet state government) and the Communist Party. The Communist Party was the only party permitted to operate within the Soviet political system and its position was enshrined in the famous (or infamous) article 6 of the Brezhnev Constitution as the "guiding and directing force of Soviet society, the nucleus of its political system". No understanding of the application of Soviet law in practice would have been complete without an appreciation of the breadth of influence that this shadow power had in the political system as a whole, and hence in the operation and interpretation of sometimes broadly permissive and flexible legislative provisions.

***The Feudal Nature of the Stalin Economic Settlement*** These general principles can be summarised by viewing the Soviet state as a dictatorship of the proletariat based upon state ownership and control of the means of production and manifested through: on the one hand, one-man management, state discipline, socialist legality and the informal controls of the

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<sup>66</sup> The *political* system was by contrast based on an ideology; and in accordance with traditional Marxist theory, this ideology informed the elaboration of the legal system based on socialist legality. It is interesting to note that the word "legality" ("*zakonnost'*") in Russian derives from the word *zakon* (meaning "positive law") as opposed to the word *pravo* (meaning "Law") - and thus socialist legality required absolute obedience to positive laws enacted by the state without further evaluation or review with reference to any "higher" notions of "Law" or "constitutionality". This is derived from the Roman law distinction between "*lex*" and "*ius*".

<sup>67</sup> See Leonard Schapiro, *The Communist Party of the Soviet Union* (Methuen & Co Ltd:1970).

<sup>68</sup> Stalin's "Short Course on the History of the All-Union Communist Party (the Bolsheviks)" published in 1938 became a classic of Soviet political literature and was compulsory reading. It was reprinted a number of times (for example, *Istoriya Vsesoyuznoi Kommunisticheskoi Partii (Bol'shevikov) - Kratkii Kurs* (Gospolizdat:1952)). A more detailed history in several volumes commenced publication in 1964 (*Istoriya Kommunisticheskoi Partii Sovetskogo Soyuza* (Izdatel'stvo Politicheskoi Literatury:1964)).

<sup>69</sup> As Lenin was quick to acknowledge, "we all know that as the governing party, we could not help fusing the Soviet structures with the party structures - with us they are fused and will so be" (43 Lenin 15).



Communist Party; and, on the other hand, an opportunity for incentivisation and devolved decision making, effected by way of the principles of democratic centralism and *khozraschet*. In this way a balance between centralising and decentralising principles was constructed around the central spine of the Stalin economic settlement, namely state ownership and state control of the means of production.

For the purposes of understanding its influences on the foundations of the law on industrial organisations, it is helpful to conceive of this settlement not just in terms of a comparison with *existing* common and civil law systems, but with the legal system of English feudalism and its legacy. Although the author knows of no examples of a comparison having been made between English feudal law and the Soviet spine of state ownership, the similarities are self-evident once suggested. Indeed Plekhanov had warned Lenin as early as 1904 that his ideology confused "a dictatorship of the proletariat with a dictatorship over the proletariat";<sup>70</sup> and early critics of the Soviet regime actually referred to it specifically as "military-feudal exploitation", "party feudalism", "a formless conglomerate constituted from feudal princedoms, amongst which we would name the "Pravda" princedom, the VTsSPS princedom, the princedom of the secretariat of IKKI, the princedom of NKPS, the princedom of VSNKh etc".<sup>71</sup>

As in the English feudal regime,<sup>72</sup> Soviet power politics and ideology attempted to vest ownership of all the means of production of the Soviet economic system in a single source, *fisc* or *weal*. In the feudal system, the means of production comprised only land, and the single source was the king. Despite possible early origins in *comitatus*, the *patrocinium*, the *precaria* and grants by the crown in the Merovingian dynasty in France, the English feudal system can be primarily traced to the conquest of England by William the Conqueror in 1066 and hence his acquisition by conquest of all land. There was no possibility for allodial holdings thereafter.<sup>73</sup> Chief lords were then "allocated" land in return for the incidents of that tenure,<sup>74</sup> originally the knight service,<sup>75</sup> and they, in turn "subinfeudated" their holdings to

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<sup>70</sup> In his article "Centralism or Bonapartism" (G.V. Plekhanov, *Sochineniya*, vol xiii, p.90-91). The final chapter of Trotsky's "Our Political Tasks" was also titled "The Dictatorship over the Proletariat" (quoted in E.H.Carr, *The Bolshevik Revolution 1917-1923, Volume One* (1950, reprinted Macmillan:1978), p.32-33).

<sup>71</sup> *KPSS v Rezolyutsiyakh i Resheniyakh S'ezdov, Konferentsii i Plenumov TsK, Chast' II* (Gosudarstvennoe Izdatel'stvo Politicheskoi Literatury:1954), p.558, 562.

<sup>72</sup> See J.L. Bolton, *The Medieval English Economy 1150-1500* (J.M. Dent & Sons Ltd:1980), and M.M.Postan, *The Medieval Economy and Society* (Penguin Books:1972).

<sup>73</sup> M.T. Clanchy, *England and its Rulers 1066-1272* (Fontana Press:1983), p.82.

<sup>74</sup> "Tenure belongs to a smaller world in which there is no need and no room for abstract ideas like ownership. Rights are dependent upon a lord seen as having total control of his lordship. A tenant is in



"mesne" (or middle) tenants in return for services to them. This produced chains of land-"holding" while preserving a single "owner" of all land (ie the King).<sup>76</sup> In legal terms, 1917 can be viewed as Russia's 1066. Russia was still an agrarian economy and it was perhaps therefore no coincidence that among the first decrees that Lenin famously adopted on 8 November 1917 were those "On Land" and "On Peace". In the same way that the Soviet state had seized power in 1917, promising peace and taking eventual control over the means of production, so too had the feudal English crown in 1066.

While the feudal analogy should not be stressed in all aspects and a detailed comparison of these two systems is beyond the scope of this study, the similarities between them are instructive in assisting an understanding of a legal system predicated upon a single owner of the means of production (the king or the state); with many holders of tenures (vassals or enterprises); and where the means of production (land in the feudal case, the industrial economy and land in the Soviet case) are allocated without ownership to others (thereby giving rise, in the feudal case, to the lord-tenant relationship through subinfeudation; and in the Soviet case, the state-state enterprise relationship through operative management<sup>77</sup>). While the feudal relationship was defined by "incidents" of tenure, the socialist relationship was defined by different "incidents" imposed by the state, namely obligatory *administrative* instructions prescribed pursuant to a state plan. And in this way the Soviet legal system contemplated both "administrative law" or "economic law" relationships (a product of the logic of the quasi feudal ownership system) and "civil law" relationships, marking the traditional balance between economic and civil law, instruction and contract, centralisation and "democracy".

### 2.3 The Soviet Law on Ownership

The feudal framework of "tenures" was reflected in the Soviet law on ownership through the concepts of "forms of ownership" and "operative management". A theoretical evaluation of this system has been left for subsequent Chapters, and for present purposes, this Section

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by the lord's allocation. He can have no more by way of title, unless it is some obligation on the lord to keep him in, or to admit his successors. He cannot by his own transaction confer whatever title he has upon another. And he cannot by himself engage in dispute about the land: in principle, the lord must decide who is to be his tenant." (S.F.C. Milsom, *Historical Foundations of the Common Law* (2<sup>nd</sup> ed., Butterworths:1981), p.100).

<sup>75</sup> A.L.Poole, *Domesday Book to Magna Carta 1087-1216* (2<sup>nd</sup> ed., Oxford University Press:1955), p.15.

<sup>76</sup> Indeed the present system of English land law is still based upon the concept of tenures. The freeholder while "holding" the "fee simple absolute in possession" is still seised of the land which "escheats" to the crown *propter defectum sanguinis* and *propter delictum tenentis* (Charles Harpum, *Megarry & Wade, The Law of Real Property* (6<sup>th</sup> ed., Sweet & Maxwell: 2000), p.17).

<sup>77</sup> See *infra* Section 2.3.1.



presents a summary of the basic positive law with a view to understanding the role, or more properly the absence of the role, of the "nature of the ownership interest" in traditional Soviet law. This is then further developed in Section 2.5.

Market orientated legal systems traditionally adopt the concept of the "generic owner"<sup>78</sup> upon which is developed a "law of property". On this basis, different legal regimes may apply to different types of property. Rights of any owner are then defined by reference to the relationship between the generic owner and the property, and most importantly whether the rights comprising that relationship amount to "title".<sup>79</sup>

The emphasis in the Soviet legal system lay elsewhere. In contrast to a "law of property" based on the generic owner and title, Soviet law developed a "law on ownership" which prescribed different ownership regimes depending upon the "identity" of the particular owner (irrespective of the type of property in question).

The positive Soviet law on ownership was almost exclusively set out in the constitution and the 1961 FPCivL (then elaborated in the civil codes). While the theory of ownership was the subject of numerous treatises in the Soviet period, until 1990, there was no separate "act" or "law" on ownership, and there were no subordinate enactments specifically "on ownership".<sup>80</sup> This was presumably because "ownership" was viewed as a conceptual structure capable of complete elaboration in the civil codes themselves without the need for more detailed legislation.

Under Soviet law, the so-called "forms of ownership" sought to define the concept of "ownership" by reference to the *fisc* ("*dostoyanie*") and the "holding" of property by allocation.<sup>81</sup> The "form of ownership" was the ideological doctrine that lay at the heart of Soviet civil law giving legal expression to the notion of the state ownership of the means of production, state planning and the classification of subjects of civil law.<sup>82</sup> Most broadly, according to Marxist political doctrine, forms of ownership were the product of the applicable

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<sup>78</sup> All owners irrespective of their identity are considered equally capable of owning rights (with limited exceptions: eg minors whose rights are curtailed generally by civil law).

<sup>79</sup> "Title is a shorthand term used to denote the facts which, if proved, will enable a plaintiff to recover possession or a defendant to retain possession of a thing...the term "absolute" is here used as meaning that the title cannot be defeated and also that it is not relative" (F.H. Lawson and Bernard Rudden, *The Law of Property* (2<sup>nd</sup> ed., Clarendon Press:1982), p.44 and 45).

<sup>80</sup> On the 1990 Ownership Law, see *infra* Chapter 7, in particular Section 7.4.

<sup>81</sup> *Supra* n.4 (1982), pp.210-212.

<sup>82</sup> *Supra* n.27 (1958), p.269, distinguishing between the economic and legal meanings of the term "ownership".



stage of societal development: the socialist mode of production gave rise to a particular economic system based on the socialist form of ownership, in contrast to private ownership that existed under the capitalist mode of production.<sup>83</sup>

Civil legislation attempted to reduce this political theory to the legal by providing for two principal forms of ownership: socialist ownership and personal ownership.<sup>84</sup> As aforementioned, whether any property fell within socialist ownership or personal ownership *depended primarily on the identity of the owner* - thus the concept of "forms of ownership" provided the doctrinal basis for distinguishing different regimes for the owning of identical objects by different owners. The law thereby protected the ownership of different owners in relation to the same types of property in different ways.<sup>85</sup>

By contrast with the forms of ownership, the "right of ownership" was the manifestation of that economic base or mode of production in the form of positive rights.<sup>86</sup> The scope of any "right of ownership" was defined by Soviet law in terms of the traditional Romanist triad: the right of possession, use and disposition.<sup>87</sup> This characterisation was inherited from pre-revolutionary Russian law;<sup>88</sup> and Soviet civil law provided that these rights of the owner arose "within the limits established by law".<sup>89</sup> As in other areas of Soviet law, the existence of the right of ownership did not necessarily imply the factual exercise of that right by the owner. For example, while the state had the "right" of ownership (including the right of possession)

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<sup>83</sup> As Marx observed "The sum total of these relations of production constitutes the economic structure of society, the real foundation, on which rises a legal and political superstructure and to which correspond definite forms of social conscience" (quoted in Maureen Cain and Alan Hunt, *Marx and Engels on Law* (Academic Press:1979), p.52). For "in [Marx] saying that a person is determined by his class status one really says that man becomes a predicate of his property" (Shlomo Avineri, *The Social and Political Thought of Karl Marx* (Cambridge University Press:1988), p.27).

<sup>84</sup> 1961 FPCivL, articles 20 and 25. See N.D. Egorov, *Tipy, Vidy i Formy Sobstvennosti i Prava Sobstvennosti v SSSR*, *SGiP* (1985), no.5, p.60.

<sup>85</sup> Depending on the applicable form of ownership involved (and hence the identity of the owner), different criminal penalties were imposed for illegally interfering with the ownership of different owners (see *infra* n.939). There were however certain types of property that could only be owned by a specific identified owner. For example, the Brezhnev Constitution listed certain property that could only be owned by the state (see *infra* n.96).

<sup>86</sup> See *supra* n.27 (1958), pp.274-276 for a summary of the principal schools of thought within traditional Soviet law as to the nature of the right of ownership; and pp.278-281 on the concept of private ownership.

<sup>87</sup> The *ius utendi*, the *ius fruendi* and the *ius absutendi*.

<sup>88</sup> The triad was referred to by Shershenevich (G.F. Shershenevich, *Uchebnik Russkogo Grazhdanskogo Prava* (1907, reprint Spark:1995), p.166) and was in the pre-revolutionary Digest of Laws (volume X(1), article 420).

<sup>89</sup> 1961 FPCivL, article 19; and RSFSR CC, article 92.



of land (all of which was in state ownership), actual possession however could have been granted to a state enterprise for a temporary period of time.<sup>90</sup>

### 2.3.1 *State Ownership and Ownership of State Enterprises*

Socialist ownership was divided into (i) state (all-people's) ownership; (ii) collective farm-cooperative; and (iii) trade union ownership. While these various forms and kinds of "ownership" were all considered to be "socialist ownership", article 11 of the Brezhnev Constitution specifically prescribed state ownership to be "the basic form of socialist ownership".

This is entirely consistent with the argument that the feudal spine of Stalin economic settlement comprised principally *state* ownership and control over the means of production and the *allocation* of state resources to enterprises and others *without the right of ownership*. Developing this reasoning, it shall be argued that the "forms of ownership regime" was an attempt to consolidate the principal place of state ownership within the Soviet economy; and, more importantly, was designed to identify the "permissible" exceptions to the principle of state ownership and to restrict the scope or availability of such exceptions.<sup>91</sup>

Although state ownership is perhaps best understood by reference to the feudal system, it was born of the theory, not of *state* control, but of "*all-people's* control" - the means of production were expressed to be held as "the common *fisc* of all soviet people"<sup>92</sup> and as a consequence it was regarded that the exploitation of man would be avoided,<sup>93</sup> and the proper development of the socialist state and the increasing wealth of Soviet citizens would be assured.<sup>94</sup> However because the Soviet state was treated by definition in the Brezhnev Constitution as "an all-people's state" where class conflict had been eliminated, there was in theoretical terms no difference between state ownership and all-people's ownership and hence the use of the term "state (all-people's) ownership" in the Brezhnev Constitution.<sup>95</sup>

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<sup>90</sup> *Zemel'noe Pravo* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1949), pp.161-175. This distinction became important in the context of the third expression of the participation model (see *infra* Section 6.5.4).

<sup>91</sup> This is examined in more detail *infra* Section 7.4.2.1.

<sup>92</sup> Brezhnev Constitution, article 11.

<sup>93</sup> *Konstitutsiya SSSR Politiko-Pravovoi Kommentarii* (Izdatel'stvo Politicheskoi Literatury:1982), p.61.

<sup>94</sup> *Kommentarii k GK RSFSR* (Izdatel'stvo Yuridicheskaya Literatura:1969), p.132.

<sup>95</sup> On the fragmentation of the concept of the "all-people's state" see *infra* Chapter 6 generally and Section 7.3 *et seq.*



The Brezhnev Constitution and the civil codes listed property that comprised exclusively state ownership. This included ownership of land and other natural resources, the basic means of production in industry, construction and agriculture, means of transport and communications, banks, property of trade, municipal and other enterprises organised by the state.<sup>96</sup>

While the form of "state ownership" established the state as *fisc*, it was the concept of "operative management" that provided the legal mechanism by which tenure was allocated to state enterprises without passing ownership.<sup>97</sup> As with ownership, "operative management" also conferred on the operative manager the triad of rights, namely possession, use and disposition. However, while the rights of the owner were limited only by law, the rights of the holder of property by way of operative management could be restricted further, by limitations placed by the owner itself.<sup>98</sup>

Under Soviet law, the concept of the ownership by the state "of a state enterprise" was relatively simple because, although the state enterprise was a juridical person and hence a subject of civil law, it was at the same time treated as an *object* of state ownership.<sup>99</sup> An enterprise therefore was simply *an indivisible object* of the law on ownership and this treatment can be traced back to the Soviet decrees of war communism years on the lease of "an enterprise".<sup>100</sup> Therefore, in accordance with the Brezhnev Constitution, "enterprises organised by the state" were expressed to be "*located in* (*"nakhodyatsya"*) the exclusive ownership of the state".<sup>101</sup> This was confirmed by their treatment in the RSFSR CC, which included "enterprises" within article 95 which set out the "Objects of the Right of State Ownership".

### 2.3.2 Other Forms of Ownership - Exceptions and Origins

In addition to state ownership, Soviet law recognised collective farm-cooperative ownership, trade union ownership and personal ownership - the former two kinds were also designated

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<sup>96</sup> Brezhnev Constitution, article 11; See also, 1961 FPCivL, article 21 and RSFSR CC, article 95.

<sup>97</sup> Operative management is considered in more detail infra Section 3.4.2. See generally, Yu.K.Tolstoi, *Sotsialisticheskaya Sobstvennost' i Operativnoe Upravlenie in Problemy Grazhdanskogo Prava* (Izdatel'stvo Leningradskogo Universiteta), p.39. Apart from state property in the industrial economy allocated by means of operative management, the other principal element of the means of production was land. Again, in common with the feudal principle, Soviet law also provided for the allocation of land without ownership through the concept of "grants of use" (see, *Sovetskoe Zemel'noe Pravo* (Yuridicheskaya Literatura:1986)).

<sup>98</sup> *Khozyaistvennoe Pravo* (Izdatel'stvo Yuridicheskaya Literatura:1967), pp.63-66.

<sup>99</sup> The mechanism *by which* state enterprises held property is considered at length within the confirmation model infra Section 3.4.2 and 7.4.

<sup>100</sup> Infra Section 6.1.4.

<sup>101</sup> Brezhnev Constitution, article 11 [emphasis added].



"socialist ownership". It has been argued that all of these "other" forms should be regarded as "exceptions" to the spinal principle of ownership residing in the *fisc* (ie state ownership), and allocation to subjects of civil law by way of operative management or for use, in each case without ownership.

The origins of these "exceptions", and indeed the treatment in Soviet law of the industrial organisation as separate from the agricultural organisation, can be regarded as a product of the early history of the Soviet regime. The forms of ownership reflected the key battlegrounds of the emerging Stalin economy of the late 1920s and early 1930s. Each form (other than that of state ownership) had a corresponding interest group that needed to be defined and confined to ensure the victory of the Stalin socialist state and economic settlement. Through identifying and regulating each of these exceptions as a separate "form of ownership", the Stalin state could effectively limit the scope of ownership (and hence economic power) of each exception.

The agriculture/industry and peasant/worker distinctions can be traced as far back as the Petrine reforms and the early debates in Russian history between the Slavophiles and the Westernisers. By the late nineteenth century, the organisation of agriculture and the related peasant question, and the industrialisation of Russia generally, became two principal policy issues for the Tsarist regime. The distinction between agriculture and industry found its way into Russian Marxist revolutionary thinking of the time which was split between those who regarded the peasant as the revolutionary class (such as the *narodniks*) and those who rather turned towards the proletariat (such as the Russian Social-Democratic Workers Party, later to evolve into the Bolshevik Party).

This legacy was taken up by Lenin as early as 1904 in his "Two Tactics of Social Democracy in the Democratic Revolution".<sup>102</sup> Lenin saw the proletariat as the universal class, but realised that only a "a revolutionary-democratic dictatorship of the proletariat and the peasantry" would be able to overthrow the existing bourgeois government. On this basis, the early decrees of the Soviet government stressed the concept of an "alliance" between the proletariat and the peasantry.<sup>103</sup>

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<sup>102</sup> 11 Lenin 1.

<sup>103</sup> A "provisional workers' and peasants' government" was to be established by the decree "On Peace" (supra n.26 (1957), p.46); the "Declaration of Rights of the Toiling and Exploited People" opened with the words "Russia is declared a republic of Soviets of workers', soldiers' and peasants' deputies" (ibid, p.102); and article 9 of 1918 RSFSR Constitution referred to the "establishment of the dictatorship of the urban and rural proletariat and the poorest peasantry...". Indeed the split and alliance between the peasant and worker as different elements of the Soviet state survived into the preamble to the Brezhnev Constitution which referred to the USSR as an "alliance of the working class, collective farm peasantry and people's intelligentsia".



Following the end of the civil war and the consolidation of Soviet power, it became clear that the policy requirements of agriculture and industry were seemingly mutually exclusive and yet the development of both was key to the success of the Soviet regime. Like the opening and closing of Trotsky's scissors, official policy throughout the 1920s vacillated, first in terms of NEP (the policy of "facing the countryside" and the so-called "wager on the kulak") and then in terms of industrialisation and the planned economy (the policy of "favouring" the proletariat coupled with the socialist industrial offensive and collectivisation of agriculture).

The development of collective farm-cooperative ownership and personal ownership as exceptions to the feudal principle of state ownership reflected two principal battlegrounds in the emerging Stalin economy - between the demands of industry on the one hand, and those of agriculture and the individual/the collective farm household (the "*kolkhoznyi dvor*") on the other.<sup>104</sup>

The legacy of the Tsarist state and the "peasant question" resolved during the struggles for the establishment of a "socialist" economy during the 1920s and 1930s gave rise to a different economic settlement for industry and agriculture. Within agriculture, the emergence of the central place of the "artel form" of collective farm symbolised that fact that the Soviet polity was prepared to recognise the personal interests of the collective farmers (or former Tsarist household farm (the "*dvor*")) as separate from those of the collective farm as a whole.<sup>105</sup> And it was this separation of interests that perhaps ultimately gave rise to the possibility for two distinct exceptions to the basic principle of state ownership.

#### 2.4 Collective Farms, Ownership of Collective Farms and Personal Ownership

While the status and law of collective farms may not seem to be of direct relevance to the law on industrial organisations (and indeed such a link has to the knowledge of the author never

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<sup>104</sup> In the same way as the history of the collectivisation of agriculture and the rights of the *dvory* were instrumental in the development collective farm-cooperative and personal ownership, the history of the independent trade union movement led by Tomskey and its overthrow were probably instrumental in explaining the "third exception" to state ownership, trade union ownership.

On the potential threat of the independent trade union movement to the consolidation of centralised Soviet power and its eventual defeat in the late 1920s see, E.H.Carr & R.W.Davies, *Foundations of a Planned Economy 1926-1929, Volume One (II)* (1969, reprinted Macmillan:1978), chapter 20. It was perhaps due to this threat that the Stalin Constitution did not reserve a specific category for the ownership of trade unions and other social organisations. By the time of the adoption of the Brezhnev Constitution, the ubiquity of Soviet power had been established and trade unions had effectively been absorbed into the Soviet state structure. The Brezhnev Constitution recognised for the first time the ownership of trade unions and other social organisations as a specific form of socialist ownership in its own right, perhaps as a legacy of another key battleground of the 1920s and its effective neutralisation at the hands of the Stalin and Brezhnev states.

<sup>105</sup> On the artel and the history of cooperatives and the collective farm, see *infra* Sections 2.4.1 and 6.1.3.



been made in Soviet or western legal literature or doctrine), it shall be shown in later Chapters of this study that the law of collective farms and its attendant ownership regime can be regarded as of decisive significance for the structure and models of the *perestroika* era industrial organisations. This Section sets out the basic background necessary for the elaboration and exploration of this link.

It may be most appropriate to regard the right of the Soviet collective farm to own property in its own separate capacity as a product of its history and the legal compromises made by the Soviet state during the process of the collectivisation of agriculture. The massive disruption to peasant life as a consequence of the collectivisation drive has been well documented. The strategy of the Soviet regime was neither entirely reasoned in advance of the last months of 1929, nor did it represent a continuing uninterrupted progression; rather the collectivisation effort resulted from brutal coercion punctuated by restraint, remorse and the re-assertion of the voluntary principle of which Stalin's article "Dizzy with Success" of 19 March 1930 was perhaps the most famous example.<sup>106</sup> The resulting legal framework found some stability with the adoption of the "Stalin Agricultural Artel Charter" in February 1935,<sup>107</sup> however as Davies rightly commented: "this was not a unified or even a coherent system, but a mixture of different systems and devices, traditional and new, introduced piecemeal in the course of the struggle to adapt the individual peasant to the new collective way of life".<sup>108</sup>

#### ***2.4.1 The Collective Farm and Collective Farm Ownership - A Combination of Social and Personal Interests***

The essence of the collectivisation compromise was embodied in the legislation on collective farms. At its heart, collective farm law was essentially based on the principle of "the combination of social and personal interests".<sup>109</sup> While the nature of the social interests on the one hand, and the personal interests on the other, were not specifically set out in the legislation or textbooks, the "combination of...interests" can be summarised as set out below. The compromise was best illustrated by reference to the provisions of the 1935 Artel Charter which was drafted while the impact of collectivisation was still very real in peoples' minds. The later 1969 Collective Farm Charter, while embodying the same compromise, reflected

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<sup>106</sup> 12 Stalin 191.

<sup>107</sup> *Sbornik Zakonodatel'stva po Sel'skomu Khozyaistvy, Tom I (Rassylaetsya po spisku)* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1955), p.139.

<sup>108</sup> R.W.Davies, *The Soviet Collective Farm, 1929-1930* (Harvard University Press:1980), p.167.

<sup>109</sup> *Kolkhoznoe Pravo* (Gosyurizdat:1950), p.22.



more of the underlying reality, namely the state's ability in practice "to trump" many of the formal legal "rights" of the collective farmers.

- **"Social Interests"** The basic interest of "the social" (ie the Soviet state) was to retain *de facto* control over the agrarian economy while at the same time legitimating the collectivisation drive by characterising it, in ideological terms, as "voluntary" and stressing that the "rights" of collective farmers were "achieved" through their rejection of the pre-revolutionary agricultural settlement and their embrace of the collective farm compromise. As such, collective farms were characterised as "voluntary" associations,<sup>110</sup> and the legislation used the term "social interests" as a euphemism for "state interests", and "socialisation" as a euphemism for "nationalisation".<sup>111</sup>
- **"Personal Interests"** The basic interests of "the personal" (ie the personal interests of the individual collectivised peasants and *dvory*) were characterised initially as the right to retain a certain level of autonomy of operations; to receive compensation for work done; and to retain a personal landholding separate from the collective farm, which could be farmed for the exclusive benefit of the *dvor*.
- **The Artel and Personal Ownership** While the 1922 RSFSR Land Code contemplated various cooperative forms of collective agriculture, following the first mass collectivisation drive of October 1929-March 1930, Stalin chose the artel form to be the

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<sup>110</sup> See A.K.R Kiralfy, *The History of Soviet Collective Farm Legislation*, in W.E. Butler (ed.), *Russian Law: Historical and Political Perspectives* (Oceana:1977), p.196: "The "voluntary" character of collectivization was always officially stressed, even in the days of forced collectivization".

<sup>111</sup> On the origins of the "socialisation principle" in this area, see supra n.22 (1948), pp.686-690 and 702-704. "Socialisation" as a concept was initially devised by the social revolutionaries as a term for placing all land in the "public domain" without state or private ownership. It was used by Lenin in the earliest days of Soviet power to attract a broad range of interest groups to the Bolshevik cause against the Tsarist supporters. Fundamentally however Lenin was against the concept, as his Bolshevik state was to be constructed specifically on state ownership (and not its absence). On the use of "socialisation" in the initial decrees on land in 1917-1918 Lenin pragmatically commented "it does not matter that our first decrees were written by social revolutionaries...when carrying out this decree the soul of which was in "socialisation" of land, the bolsheviks have stated precisely: it is not our idea, we do not agree with such a slogan, but we consider it to be our duty to carry it out because it is demanded of the prevailing majority of peasants" (quoted by Gsovski, *ibid*). And indeed the use of the term "socialisation" in relation to land was dropped as early as February 1919 when the decree "On Socialist Land Construction and on Measures to Transferring to Socialist Agriculture" referred in article 1 to land as "a single government reserve" (*Resheniya Partii i Pravitel'stva po Khozyaistvennym Voprosam, Tom 1* (Izdatel'stvo Politicheskoi Literatury:1967), p.109).

Although socialisation was rejected by the Bolsheviks in favour of centralisation of power through nationalisation and state ownership, ideologically it again provided a pragmatic solution to the legal characterisation of the collectivisation process. The term "socialisation" survived in the context of collective farms, and was specifically referred to in the 1935 Artel Charter and the 1969 Collective Farm Charter. See infra n.116.



basis for the development of collective farming and this was embodied in the 1935 Artel Charter.<sup>112</sup> The artel form represented a balance between the social and personal interests: assets of farmers were transferred to the collective farm (and split between an indivisible fund and a share fund). However, farmers did retain the right to certain assets for their personal use.<sup>113</sup> Both the 1965 Artel Charter in Section III and the 1969 Collective Farm Charter in Section X contained detailed provisions on the right of the *dvor* to retain the use of a personal land plot and the right of the *dvor* to own property that could be used in connection with the farming of that personal plot (including a dwelling and agricultural implements). These separate rights of the *dvor* required legal expression and hence the necessity to provide for a "form of ownership" separate from "state ownership". This may therefore have been in part the origin of "personal ownership"<sup>114</sup>. Thus the artel form at its core illustrated the collective farm law compromise where the former peasants and members of pre-revolutionary *dvory* were collectivised but at the same time were given the formal legal right to carry out certain limited "personal" agricultural operations and to own assets connected with the performance of such operations.

- **Collective Farm Ownership** The collective farm created in the form of the artel was given the status of a juridical person and, in contrast to state enterprises, was given the right of ownership of property "needed for them to carry out charter tasks"<sup>115</sup> - ie collective farm-cooperative ownership. This can be viewed as another exception to the principle of state ownership of the means of production and was probably designed to evidence the "voluntary" principle. While the means of production in the *industrial* economy were simply nationalised into state ownership, the Soviet state "seizure" or collectivisation of the *agrarian* economy was more complex, and needed to be "legitimated" or "veiled" by means of a different legal framework. Thus the property of the members of the collective

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<sup>112</sup> See infra Section 6.1.3 as to the other forms of cooperation provided in the 1922 RSFSR Land Code: the artel was in fact the compromise form (joint tillage resulted in shared use of only the basic equipment, but otherwise farmers operated autonomously; and the agricultural commune resulted in pooling of *all* assets and income). The artel had its origins in the pre-revolutionary "workingmen's cooperatives" and also formed the basis for the simple partnership of the industrial economy as set out in the 1922 RSFSR Civil Code (infra Section 4.1).

<sup>113</sup> Supra n.109, p.8.

<sup>114</sup> "Personal ownership" was also seen as the "socialist" successor to the capitalist form of "private ownership" (see infra Section 2.4.3).

<sup>115</sup> Brezhnev Constitution, article 12. Property exclusively in state ownership could not be in collective farm-cooperative ownership, but could be allocated to the collective farm for use (eg land). See *Zakonodatel'stvo ob Immushchestvennykh Pravax i Obyaznostyakh Kolkhozov (Izdanie Numerovannoe - Rassylaetsya po Spisku)* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1953).



farm was characterised as having been "socialised" into the "social ownership" of the collective farm, regulated by the form of collective farm-cooperative ownership: Doctrinally the former assets "of" the *dvor* (in which the peasants in a household were members) were transferred/socialised into the "social" ownership of the collective farm (in which those peasants then became members) and not into the ownership the state itself.<sup>116</sup>

- **Membership, Fees and Funds** On joining a collective farm, peasants became "members". This was expressed to be "voluntary". The 1935 Artel Charter provided for the following payments that were associated with membership ("*chlenstvo*"):<sup>117</sup>
  - an entry fee ("*vstupitel'nyi vnos*") of between 20-40 rubles was payable to the "indivisible fund" ("*nedelimi fond*") of the collective farm; and
  - "socialisation" of a half to a quarter of the property of a member by way of transfer of such property to the indivisible fund; and "socialisation" of most of the remainder by way of transfer of such property to the "share fund" ("*paevoi fond*"). The wealthier peasants had a greater share of their property transferred to the indivisible fund. All land was transferred to the indivisible fund.

A member had the right to withdraw from a collective farm whereupon his share ("*pai*") of the share fund (but not of the indivisible fund) would be transferred back to him. The voluntary nature of collectivisation was therefore underlined in the legislation by the right to withdraw, and the fact that only a certain portion of the former holdings of the *dvor* was irrevocably socialised (ie the property transferred to the indivisible fund) and that the rest was potentially available for return.

- **Collective Farm Democracy** The origins of the democratic process in agriculture can be traced to the pre-revolutionary *mir* (or assembly) constituted by *dvory* where the heads of the households attended the *skhod*. The administration of the Soviet collective farm developed from these institutions and indeed, in early collective farm legislation, the chairman was actually called the "*starosta*" (the elder). The collective farm legal literature explained that the 1935 Artel Charter was based on "collective farm

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<sup>116</sup> Supra n.111. The 1935 Artel Charter set out specifically a list of property of the collective farmers that was to be "socialised" upon joining the collective farm and stated that the remaining property was to be "in the personal use of the collective farm household (*dvor*)" (articles 4 and 5). The 1969 Collective Farm Charter also referred to the "social ownership of the collective farm" (Section IV). On the early socialisation of the property of the *dvory* into the ownership of the collective farm, supra n.108, pp.68-115.

<sup>117</sup> 1935 Artel Charter, articles 9 and 10.



democracy", "the principle of broad autonomy of the collective farm mass and the election of organs of administration arising from the essence of the collective farm as a voluntary organisation of peasants and democratic fundamentals of the administration of the collective farm."<sup>118</sup> The principal organs were the general meeting of the collective farmers, a board and a chairman (elected by the general meeting), and an audit committee. Various basic powers and procedures for calling meetings were also set out in the charters.<sup>119</sup>

- ***Personal Participation, Payment and Incentives*** In contrast to the payment of workers in state enterprises who received fixed wages, the collective farm wage structure was based on the principle of developing a "material interest of the collective farms and the collective farmers in the results of their labour".<sup>120</sup> Personal participation in the activity of the collective farm was an obligation,<sup>121</sup> and wages were initially linked to the number of "labour days worked".<sup>122</sup>
- ***Coercion and State Control*** State control over the activities of the collective farm was in practice almost absolute despite the "compromise" of the artel form which seemingly provided for the "autonomy" of the collective farmer evidenced by voluntarily accession to the collective farm; the right of withdrawal and the return of property socialised by way of transfer to the share fund; the right to participate in decision making; the right to receive a portion of the profits; and the right to a personal land plot. After the consolidation of the collectivisation drive in the 1940s and 1950s, state control was gradually extended, and the 1969 Collective Farm Charter reflected more accurately the situation in practice and reality.

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<sup>118</sup> Supra n.109, p.21.

<sup>119</sup> See 1935 Artel Charter, Section XI (Organs of Management and Audit Commission of a Collective Farm) and 1969 Collective Farm Charter, Section VIII (Administration of Activities of the Artel). See generally, I.V.Pavlov, Ponyatie i Sushchestnost' Kolkhoznykh Pravootnoshenii i Rol' Organov Upravleniya i Formirovaniya i Razvitiya Etikh Otnoshenii, in *Voprosi Kolkhoznogo i Zemel'nogo Prava* (Izdatel'stvo Akademii Nauk SSSR:1951), p.73.

<sup>120</sup> *Kolkhoznoe Pravo* (Yuridicheskaya Literatura:1970), p.17.

<sup>121</sup> 1935 Artel Charter, article 13, and 1969 Collective Farm Charter, articles 5 and 24.

<sup>122</sup> 1935 Artel Charter, article 15. On early law of payment for labour in collective farms see, supra n.119, p.257. On the origins of the labour day principle, see supra n.108, chapter 7. The labour day payment procedure eventually gave way to a more general test of "quantity and quality of labour" as set out in 1969 Collective Farm Charter, article 27.



The legal and ideological doctrines which suggested that collectivisation was voluntary were not of course supported by the history of the 1920s.<sup>123</sup> In any event, by the 1970s, the creation of collective farms by voluntary means (ie at the initiative of collective farmers) was described in textbooks as part of their initial historical origin, and that in "current times" new collective farms were only permitted to be established by way of merger or division of existing farms.<sup>124</sup> Termination of collective farms was only really considered in the context of a possible transformation into a state farm;<sup>125</sup> and while the principle of withdrawal was still implicitly referred to in article 7 of the 1969 Collective Farm Charter, there was no mention of the share fund or the right to receive a portion of it upon withdrawal. As one textbook explained: "the relationship between the indivisible funds and the share fees became entirely changed. The specific weight of the former increased uninterruptedly, while the latter fell; and in the final account, the former became maximised, nearly all-encompassing and the latter insignificant".<sup>126</sup>

The 1969 Collective Farm Charter embodied a doctrine that more appropriately reflected reality. The indivisible fund/share fund distinction was simply ignored and was replaced by the more usual distinction used in industrial organisations, between basic and circulating funds,<sup>127</sup> which was described to be "the real state of affairs".<sup>128</sup> The

<sup>123</sup> On the creation of collective farms Ioffe rather cynically commented: "now it is known all over the world that collective farms were created not on the initiative of the peasants, in conformity with the law, but by illegal coercion directed by Stalin and his henchman..." (Olimpiad S. Ioffe, *Soviet Civil Law* (Martinus Nijhoff Publishers:1988), p.35). Ioffe clearly presented a relatively simplistic view of the extremely complex history of the collectivisation of agriculture. The early collective farms in the period to 1928 were small scale and generally voluntary in nature. There was little sometimes to distinguish them from agricultural cooperatives. It was only later with the collectivisation drive that coercive elements became more widespread, particularly for the period from November 1929 to March 1930. Following Stalin's "Dizzy with Success" article in March 1930, the voluntary principle was seemingly restored (See, R.W.Davies, *The Socialist Offensive, The Collectivisation of Soviet Agriculture, 1929-1930* (Macmillan:1980), pp.110, 135, 153, 205-212, 269 and 286).

<sup>124</sup> *Kolkhoznoe Pravo* (Yuridicheskaya Literatura:1973), p.39.

<sup>125</sup> A treatise devoted to "Collective Farm Legal Relations" only had one page of text on the "Foundations of Termination of Collective Farm Legal Relations" and merely noted "sometimes individual collective farms are transformed into state farms" (A.A.Puskol, *Kolkhoznye Pravootnoshcheniya v SSSR* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1960), p.141).

<sup>126</sup> *Kolkhoznoe Pravo* (Yuridicheskaya Literatura:1972), p.233.

<sup>127</sup> 1969 Collective Farm Charter, article 12 and 1961 FPCivL, article 11. One textbook on collective farm law noted that, in addition to state aid, general production and rights under contracts, the other remaining "source" of collective farm property and funds was "socialised implements and means of production and the making of entry fees upon entering a collective farm". It then commented that "these sources of collective farm ownership had deciding importance in the organisation and creation of collective farms. In the present time, socialised means of production and entry fees as sources of formation of collective farm ownership have lost their significance...The model collective farm statute of 1969 in general does not contemplate them... The process of collectivisation in our country has long been completed" (supra



ideological veils of voluntary collectivisation, the right to withdraw and the right to repayment of a portion of contributions made to a share fund were all consigned to history as the law shifted to reveal yet again that the Soviet concept of "socialisation" was little different from outright "nationalisation".<sup>129</sup>

However, the use of the term "socialisation" did seemingly mean that, as a matter of strict legal doctrine, the collective farm did not fall within state ownership and thus the state did not have the ability to control the activities of the collective farm through its role as owner of the farm or of its property.<sup>130</sup> State control was achieved through means other than direct ownership of the collective farm, through its direction of the national economy more generally.

As regards the activities of the collective farms, although the collective farmers notionally had the right to vote in the decision making organs and had wages linked to productivity, Soviet law conceived of the collective farm as a part of the single national economic state planned network,<sup>131</sup> and this was stressed not only in the 1969 Collective Farm Charter, but also in article 10 of the Brezhnev Constitution which provided that collective farm-cooperative ownership constituted (together with state ownership) "the basis of the economic system of the USSR".<sup>132</sup> As collective farms did not operate outside the national economy, they were subject to planning discipline, and in practice therefore, their legal autonomy was significantly curtailed.<sup>133</sup> Intervention by the state in their operation was explained as follows: "the leadership of the collective farms on the part of the party and state agencies is the most sure guarantee of their development along the correct path".<sup>134</sup>

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n.120, p.147 and n.1 therein). This position was also reflected in the lists of objects of collective farm-cooperative ownership in 1961 FPCivL, article 23 and RSFSR CC, article 100 which did not mention entry fees, socialised property or property in the share fund.

<sup>128</sup> Supra n.126, p.233.

<sup>129</sup> Supra n.111.

<sup>130</sup> On the ownership of collective farms, see *infra* Sections 2.4.2, 6.4.1 and 6.4.4.2; and on the roles of the state as creator-owner and property-owner in the context of state enterprises, see *infra* Section 3.4.

<sup>131</sup> See generally, *Zakonodatel'stvo o Proizvodstve i Gosudarstvennykh Zakupkakh Sel'skokhozyaistvennoi Produktii (Dlya Sluzhebnogo Pol'zovaniya)* (Yuridicheskaya Literatura:1975).

<sup>132</sup> "Cooperative-collective farm organisations" were "an integral part of the socialist economic system of the USSR and their activities shall be determined and directed by the state national economic plan...in accordance with article 6 of the Model Charter on the agricultural artel..." (*supra* n.27 (1950), p.314).

<sup>133</sup> On the importance of the national economic plan and state control over the agrarian economy see A.I.Volkov, *O Pravax i Odyazannostyakh Kolkhozakh po Razvitiyu Obshchestvennogo Proizvodstva* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1961) and I.F.Kaz'min, *Proizvodstvenno-Khozyaistvennaya Deyatel'nost' Kolkhozov* (Yuridicheskaya Literatura:1972), pp.64-88.

<sup>134</sup> Supra n.126, p.30.



Textbooks on "collective farm law" invariably included an entire chapter on "The Legal Organisation of the State Management of Collective Farms" which stressed state control, the leading role of the party and its local organisations, and the fact that "collective farm democracy" meant a *combination* of state management with broad autonomy of the collective farm mass.<sup>135</sup> Article 14 of the 1969 Collective Farm Charter simply required the collective farm when working out its own plan to "proceed from...the fulfilment of the state procurements plan". In short, although as a legal matter, the collective farms were not owned by the state, despite the fact that they had the right to own property in their own right (unlike state enterprises) and despite the fact that collective farmers had the right to vote in management decisions, in reality, the state ultimately retained broad control over their activities.

Collective farm law was basically the most visible expression of the balances in the Soviet macro economy between economic law and civil law, plan and contract, central control and autonomy. Ultimately their legal framework was a product of their history. As Gsovski commented "the blend and equilibrium of the collectivist and private elements in the collective farms is not static but dynamic. It is a product of compromise, of trial and error, and bears the traces of the struggle from which it evolved".<sup>136</sup> However, as the Soviet state consolidated its control over the agricultural sector during the 1940s and 50s, the balance shifted in favour of the state or "socialising processes" and as has been shown, the essence of the collective farm became an association with certain formal legal rights for its members but incorporating systemic and specific over-riding mechanisms by which the Soviet state retained effective control. By abolishing the share fund and referring to the plan, the 1969 Collective Farm Charter moved the legal position closer to the underlying reality but still incorporated the formal legal fundamentals of the traditional framework. It is perhaps for this reason that Ioffe

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<sup>135</sup> See for example, supra n.109, chapter IV; n.124, chapter 3; supra n.126, chapter V; Prof.V.N.Dem'yanenko, *Kolkhoznoe Pravo* (Saratov:1972), chapter 4. On the role of the party and state generally in leading and directing the collective farms on the basis of a unified state and economic administration, see *Pravovye Problemy Rukovodstva i Upravleniya Sel'skim Khozyaistvom v SSSR* (Izdatel'stvo Nauka:1970), pp.57-91. On the nature of the normative legal enactments promulgated by the party and state in "directing" the collective farm movement, see Z.S.Belyaeva, *Istochniki Kolkhoznogo Pravo* (Izdatel'stvo Nauka:1972), pp.178-218.

<sup>136</sup> Supra n.22 (1948), p.724.



and Maggs noted that "the degree of fiction and fantasy is substantially higher in collective farm law than in other areas of law related to the economy".<sup>137</sup>

#### 2.4.2 *Ownership of Collective Farms*

The law of collective farms was indeed very much a fantasy world, with origins in the pre-revolutionary agrarian economy, the brutal collectivisation drive and the socialist industrial offensive. Section 2.4.1 presented the skeleton of a basic model for the collective farm, akin to those to be developed in the principal body of this study for industrial organisations. Its importance will become clearer in later Chapters. However, the question of the "ownership" of a collective farm was not directly considered.

This question was relatively quickly addressed with respect to state enterprises as they were conceived as indivisible objects of the law on ownership, "located in" state ownership.<sup>138</sup> As regards the other principal juridical person in the Soviet economy, the collective farm, the answer to the question "who owned the collective farm?" was rather unclear and, to the author's knowledge, was and never has been posed in these express terms.<sup>139</sup> The situation was not helped by the use of the phrase "collective farm ownership" ("*kolkhoznaya sobstvennost'*") in the literature as it finessed the distinction between the ownership of property *by* a collective farm; and the ownership *of* that collective farm by others.

In the absence of an explicit doctrinal exposition in the legislation, it is tempting simply to view collective farms, like state enterprises, as a type of "enterprise" also "located in" state ownership. Unfortunately article 11 of the Brezhnev Constitution rather explicitly provided that only enterprises "organised by the state" fell within state ownership, and it was relatively clear that collective farms were not organised by the state. Article 6 of the Stalin Constitution was even more instructive as it included specifically "state farms" within state ownership and did not include collective farms. Furthermore, it was doubtful whether a collective farm even constituted an "enterprise" at all. The word "enterprise" was not a term of art under Soviet law prior to 1990, however the 1969 Collective Farm Charter defined the collective farm as a

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<sup>137</sup> Olimpiad S. Ioffe and Peter B. Maggs, *The Soviet Economic System - A Legal Analysis* (Westview Press:1987), p.55.

<sup>138</sup> Supra Section 2.3.1.

<sup>139</sup> For example, the chapter in a collective farm treatise relating to the "Constitutional Foundations of Collective Construction in the USSR" considered in great detail the right of the collective farm to own property (and how this interacted with state ownership) as well as the right of the *dvor* to use a personal land plot and own property for its farming, however there was no consideration of the nature of the right of ownership of a collective farm itself and who, if anyone, did own the collective farm (I.V.Ivanov, *Ustav - Zakon Kolkhoznoi Zhizni* (Yuridicheskaya Literatura:1979), pp.10-19).



"cooperative organisation",<sup>140</sup> and not as an "enterprise"; and indeed it was very unusual to find the term "enterprise" being used to describe a collective farm.<sup>141</sup> In short, as already discussed, the collective farm was a creation of the collectivisation of agriculture whereby the former property of the Tsarist peasant households was, as a strictly legal matter, "socialised" to form the collective farms and was not "nationalised" into state ownership.

If the state did not own the collective farms, it is again tempting to assume that as a result of the socialisation process the collective farms were owned by the collective farmers. There was however no direct reference in the legislation on collective farms, nor in the law on personal ownership, that hinted at the possibility that a collective farmer could have owned a direct interest in a collective farm itself. An answer therefore is perhaps best derived through an analysis of the concept of "membership".

The concept of "membership" dated back to the pre-revolutionary customary law of the *dvor*. Following collectivisation, membership in the *dvor* was replaced by membership in the collective farm, and Soviet law provided for various incidents of membership in a collective farm which could have been interpreted as indicating "ownership of" the collective farm by its members. These included the obligation to pay an entry fee on accession; a right to vote at the general meeting; and (prior to 1969) the right to a portion of the share fund on withdrawal. Indeed the Russian word for share ("*pai*") seemed to indicate a term of art for the interest that a collective farmer owned in a collective farm. Furthermore, article 23 of the 1969 Collective Farm Charter explicitly provided that the obligations of the collective farmers were separate from those of the collective farm itself and *vice versa*. Such a rule suggested that collective farmers might have had an ownership interest of the collective farm itself, and therefore legislators thought it necessary to provide explicitly that their respective responsibilities were separate.

There was some discussion generally in Soviet doctrine about the concept of "membership",<sup>142</sup> and these early debates were no doubt bound up with the history of collectivisation and its legitimation through law. However, contemporary textbooks conceived of membership purely in terms of a series of mutual rights and obligations as between two subjects of civil law (the

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<sup>140</sup> "Organisation" was as a term of art used for any juridical person (supra Sections 2.5 and 7.5 (initial paragraphs)).

<sup>141</sup> While the collective farms were rarely described as "enterprises", the term was applied to subdivisions created by collective farms ("auxiliary enterprises") and combinations of collective farms ("Intercollective farm enterprises") (see 1969 Collective Farm Charter, articles 16 and 17).

<sup>142</sup> For an overview of the early debates, see Yu.A.Bobk, *Kolkhoznoe Trudovoe Pravootnoshenie* (Yuridicheskaya Literatura:1972), pp.5-24.



collective farmers and the collective farm) and not in terms of ownership interests. These rights therefore included the right to work, the right to receive a portion of the distributed property, the right to receive wages based on quality and quantity of work, the right to leisure, the right to material support in the case of illness or loss of an ability to work, the right to participate in management activities and others.<sup>143</sup>

The only clearly identifiable ownership interest of the collective farmer was in the "share fund" upon withdrawal under article 10 of the 1935 Artel Charter. Some textbooks argued that this right to a portion of the share fund upon a withdrawal was in any event only a contractual right,<sup>144</sup> while others acknowledged that it was a property right, but only a right in the share fund and not more generally in the collective farm itself. In any event, with the introduction of the 1969 Collective Farm Charter, the existence of the share fund was de-emphasised and this right was no longer explicitly recognised.<sup>145</sup> However, even under the 1935 Artel Charter, the fact that certain funds had always been "indivisible" and not subject to distribution to members upon withdrawal suggested clearly that any ownership interest of a collective farmer in the share fund could not have given rise *per se* to an interest in the collective farm as a whole.

In conclusion, there was no doctrinal consideration or identification of ownership interests in collective farms (beyond the question of the share fund); no clear direction in the literature on state ownership that collective farms fell within state ownership; no suggestion that personal ownership encompassed the right of members to own a collective farm; no right of members to sell, transfer or bequeath the right of membership in a collective farm; and no explicit entitlement of members to a distribution of residual funds upon termination of a collective farm (which was not even generally contemplated in textbooks). It is therefore difficult to disagree with the analysis of Bobk that "on the basis of the norms of socialist law, between the collective farm and the collective farmer arises an individual social connection, characterised

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<sup>143</sup> Supra n.126, pp.144-154.

<sup>144</sup> "As already noted in the literature, the right upon withdrawal from a collective farm to demand a return of the share fees is not a right *in rem* but a right *in personam* ("*ne veshchnym a obyazatel'stvennym pravom*")" (*Pravo Kolkhoznov Sobstvennosti* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1961), p.251).

<sup>145</sup> "Property legal relations in collective farms previously comprised relations with regard to socialised property joined to the collective farm [and] entered by way of share fees as well as participation of the collective farmers in the use of collective farm property...at the present time it has no significance, in the Model Charter of the Collective Farm 1969, socialised property on entry into a collective farm is not provided for" (supra n.124, p.11, 76).



by definite subjective juridical *rights and obligations* and guaranteed by the compulsory force of the state",<sup>146</sup> and that no ownership relationship arose between them.

### 2.4.3 *Personal Ownership*

The orthodox understanding set out in the Brezhnev Constitution was that personal ownership by citizens was "intended [to be] for their material and cultural requirements" acquired through "labour incomes".<sup>147</sup> Moreover property in personal ownership could not be used to derive non-labour income which could be seized by the state or returned to the exploited party. In addition, any property used in the production of the non-labour income could be seized without compensation.<sup>148</sup> Prevailing Soviet theory contrasted personal ownership with private ownership. Private ownership, a feature of capitalist societies, resulted in the exploitation of labour which was avoided in socialist societies through the concept of personal ownership of property (and which was actually prohibited by article 14 of the Brezhnev Constitution). As such, personal ownership represented a higher level of ownership present only in societies where class conflict was no longer existed.<sup>149</sup>

Personal ownership can also however be viewed as the final exception to the principle of state ownership of all the means of production. Its rationale, as has been argued, can be traced to the history of NEP and collectivisation: the legacy of the former meant that some degree of subsistence ownership by citizens was necessary, and the compromise effected by virtue of the latter meant that the *dvor* retained some rights of ownership within the artel form. The doctrine of non-labour income simply and conveniently confined this "exception" so as not to encroach in any significant way upon the state ownership doctrine.

## 2.5 **Ownership Interests and the Classification of Soviet Juridical Persons**

The relationship between a juridical person and its "owners" or "founders" is as a legal matter generally complex, and it is common to interpose between the "founders" and the juridical person a separate object of the law on ownership. This object of the law on ownership is typically "issued" by the juridical person, and the ownership of that object by the founders

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<sup>146</sup> Supra n.142, p.46 [emphasis added].

<sup>147</sup> Brezhnev Constitution, article 13; 1961 FPCivL, article 25; and RSFSR CC, article 105. Non-labour income was never defined in Soviet law but was understood to depend both on the legitimacy of the source of the income and the purpose for which the proceeds were applied.

<sup>148</sup> Some civil codes only had provisions relating to the seizure of property used for the *derivation* of non-labour income (eg RSFSR CC, article 111); whereas others contained an additional article for the seizure of property *acquired through* non-labour income (Kaz CC, articles 105 and 106).

<sup>149</sup> R.O.Khalfina, *Pravo Lichnoi Sobstvennosti Grazhdan SSSR* (Izdatel'stvo Akademii Nauk SSSR:1955), p.27.



gives rise to rights and obligations as between the founders and the juridical person (as well as between the owners *inter se*).<sup>150</sup> The ownership of that object by founders (rather than ownership of the juridical person itself) allows the law to finesse the "problem" of "corporate slavery" (ownership of one subject of civil law (ie a juridical person) by another (ie the founders)) and furthermore avoids the need for an explicit dual characterisation of the juridical person both as the subject and the object of the law on ownership.

For the purposes of this study, this object of the law on ownership issued by a juridical person shall be (and has been) generically called an "ownership interest" of a juridical person. An example of an "ownership interest" would be a "stock": a stock is an object of the law on ownership; and its ownership by stockholders gives rise both to an ownership relationship as between a stockholder and the stock, as well as to rights and obligations as between a stockholder and the juridical person that issued the stock.<sup>151</sup>

Ownership interests are generally distinct for different juridical persons, and different rights and obligations are associated with the owning of ownership interests of different juridical persons. On this basis, for example, a joint-stock society that issues "stocks" is distinguished from a partnership in which each partner has, for example, a "participatory share participation". The ownership interest directly reflects the nature and classification of the juridical person and also determines the form and procedure for the transfer of these interests from one owner to another.

The existence of the ownership interests is important for two principal reasons: First it is critical in focusing the legislators' mind on the nature of the relationship between the "owners" and the juridical person, and in particular on the rights and obligations that characterise this relationship. Secondly, it provides an object of the law on ownership that can form the basis for equity investment in a form that is liquid. As Clark commented "because of all these characteristics of corporate stock (free transferability of the whole bundle of rights, negotiability and fungability within classes), organized, efficient trading markets in corporate stock were able to arise and did arise".<sup>152</sup>

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<sup>150</sup> The exact nature of this property is not central to this study, however such "property" could be tangible, intangible, or even a hybrid, understood perhaps as "a bundle" of rights.

<sup>151</sup> For the concept of shares as objects of the law on ownership, see for example, in French law, article 529 of the Civil Code which characterises shares ("*les actions*") as moveables ("*meubles*"); and, in English law, section 211 of the Companies Act 1985 which refers to "interests in shares" and "rights of a person in relation to shares". Section 211 is not mentioned by Gower, but see generally L.C.B.Gower, *Gower's Principles of Modern Company Law* (Sweet & Maxwell:1992), pp.357-361.

<sup>152</sup> Robert Charles Clark, *Corporate Law* (Little, Brown and Company:1986), p.14.



As such, while the ownership interest is not a prerequisite for juridical personality,<sup>153</sup> it is probably a necessary component of a juridical person that comprises an association of capital where ownership is fragmented between various different persons and is intended to be liquid. Furthermore, it provides a basis for an initial classification of different corporate organisations and a focus for the establishment of the relationship between the owner and the juridical person.

For reasons of both function and principle, there was no concept of "the ownership interest of a juridical person" in mainstream Soviet law; and it shall be argued that this proved to be a critical structural flaw in the prevailing Soviet legal theory that undermined any precise analysis of ownership relations in the context of the new non-state owned organisations that emerged after 1987.

Within the command economy, there was only one model of the industrial organisation,<sup>154</sup> because the state owned all industrial organisations exclusively. There was therefore no need for a legal mechanism to be introduced which contemplated fragmented ownership, and the possibility for equity capital raised in the market. As such, while Russian legal terminology contained various concepts that might have been used to describe and analyse the nature of the state's ownership interest "in" state enterprises (including "*pai*" (share); "*dolya*" (participatory share); "*aktsiya*" (stocks); "*dolya uchastiya*" (participatory share participation); and "*vklad*" (contribution)), none of these appeared in the primary legislation. Soviet law simply regarded the enterprise as an indivisible object "located in" state ownership.<sup>155</sup> This did not however result in a single person being characterised both as a subject and as an object of the *law on ownership* because, due to the concept of operative management, while an enterprise was a subject of *civil law* (ie a juridical person), it was an object (and not a subject) of *the law on ownership* (ie it did not have the right of ownership).

The absence of a concept of the ownership interest within the logic of Soviet law contributed to the uncertainty relating to the legal analysis of who (if anyone) owned the other principal juridical person within the Soviet economy, the collective farm.<sup>156</sup> Soviet law finessed this question perhaps because any explicit treatment of the issue may have resulted in a call for these agricultural cooperatives to have been placed in the direct ownership of the members, thereby creating a fundamental and visible challenge to the state ownership doctrine.

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<sup>153</sup> As illustrated by the English law corporation sole.

<sup>154</sup> Infra Chapter 3.

<sup>155</sup> Supra Section 2.3.1.

<sup>156</sup> Supra Section 2.4.2.



The concept of ownership interests in juridical persons may have been absent in the case of state enterprises and finessed in the case of collective farms not just because this concept was simply unnecessary as a functional matter, but also, and perhaps more significantly, because at a deeper level it was entirely contradictory to the very foundations of Soviet civil law theory. Again it is helpful to look to the feudal analogy. In the feudal world, the concept of "owning" the means of production (ie land) was a nonsense; rather legal theory approached this relationship in terms of "seisin". Indeed the noun "ownership" was never used in the legal framework of English feudalism, and developed almost unnoticed as a consequence of the forms of action that emerged throughout the course of the thirteenth century.<sup>157</sup> As has been argued, the Soviet legal system can be viewed as having adopted a similar approach, and in common with medieval English terminology, there is no word in Russian for the verb "to own". Thus in an economy of state ownership of all the means of production, the logic of the law on ownership was based on the need to identify and regulate the scope of any exceptions to that rule,<sup>158</sup> rather than to elaborate a framework for a law of property where all subjects of civil law have the generic capacity "to own" and where the focus therefore is on the nature of the different rights that those subjects have in relation to property.<sup>159</sup>

The general definition of the juridical person was set out in article 11 of the 1961 FPCivL and took into account the fact that industrial organisations (ie state enterprises) did not have the right of ownership but were only allocated property by the state for operative management. Thus juridical persons were defined as "organisations" that had "solitary" ("*obosoblennye*") property (ie property owned by *or* allocated to it). In this way it was meaningful to talk of the property "*of*" a juridical person (ie entered into its independent budget or separate balance sheet) without it necessarily being in the ownership of that juridical person. Furthermore, juridical persons were expressed to have the capacity "to acquire" rights as well as to bear obligations. By using the word "acquire" in relation to rights (rather than "owing"), the definition enabled all juridical persons to enter into contractual relations and acquire rights, even if they did not have the right of ownership. This was consistent with the law on ownership which did not include "rights" within "objects of the law on ownership" - hence

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<sup>157</sup> See S.F.C. Milson, *The Legal Framework of English Feudalism* (Cambridge University Press:1976), pp.36-65.

<sup>158</sup> Ie the *identity* of persons other than the state that had the capacity to own (eg collective farms, trade unions, citizens). See *supra* Sections 2.3.1 and 2.3.2.

<sup>159</sup> *Supra* Section 2.3 and *infra* Sections 7.1 and 7.2.



rights *were not* capable of being owned, and therefore *were* capable of being acquired by juridical persons without the right of ownership.<sup>160</sup>

Article 11 of the 1961 FPCivL then classified juridical persons implicitly on the basis of the forms of ownership outlined above. Therefore article 11 distinguished four categories of juridical person: (i) state enterprises and other state organisations; (ii) collective farms, inter collective farms and other cooperative organisations; (iii) state-collective farm and state-cooperative organisations; and (iv) other organisations in the instances provided for by legislation of the USSR.<sup>161</sup>

Until 1985, industrial organisations almost exclusively fell in the Category (i) (state enterprises to which were allocated property in state ownership). The classification and ownership regime of the "new" industrial organisations introduced from 1987 either fell within the Category (ii) and its implicit ownership regime (eg cooperatives on the basis of collective farm-cooperative ownership), or made use of Category (iv), the catch-all category (eg leased enterprises), but this inevitably resulted in an ambiguous ownership regime because, as a catch-all category, it had no corresponding ownership form upon which it was based. While these "new" industrial organisations were situated on the edges of this matrix of ownership law, they exploited another element of the law on ownership, namely the concept of common ownership.

## 2.6 Common Ownership and Joint Activity

Common ownership was not a "form" of ownership but merely a mechanism by which property was jointly held. Thus relations between an owner and its property were characterised by a "form of ownership" whereas relations between two owners of the same property were additionally characterised by "common ownership". Not surprisingly, common ownership law was intimately connected with associations based on personal participation and facilitated their creation on the basis of pooled resources without the formation of a juridical person.<sup>162</sup> Common ownership was contemplated between juridical persons or between citizens, but not between citizens and juridical persons.<sup>163</sup>

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<sup>160</sup> On the Soviet law of rights in this respect, see *infra* n.519, 859 and 912. "Rights" only became an object of the law on ownership with the enactment of the 1991 FPCivL. Article 4 thereof on objects of civil rights included "other property, including property rights".

<sup>161</sup> Category (iv) was inserted by virtue of an amendment in 1981 (O Vnesenii Izmenenii i Dopolnenii v Osnovi Grazhdanskogo Zakonodatel'stva Soyuza SSR i Soyuznikh Respublik, *Vedomosti SSSR* (1981), no.44, item 1184).

<sup>162</sup> See *infra* Chapter 4.

<sup>163</sup> RSFSR CC, article 116.



The law of common ownership was governed by a separate chapter of the civil codes,<sup>164</sup> which distinguished "joint ownership" from "common participatory share ownership" ("*obshchaya dolevaya sobstvennost'*").<sup>165</sup>

Joint ownership could be considered as equivalent to the common law notion of "joint tenants",<sup>166</sup> each owner held an undivided interest in the whole. Under Soviet law, it was only really applicable in two instances: property held by a husband and wife which did not stem from a marriage contract; and that of a collective farm household (or *dvor*).

Common participatory share ownership could be considered as equivalent to the common law concept of "tenants-in-common".<sup>167</sup> The common property was divided into participatory shares ("*dolya*") which were allocated separately to the individual owners. The owners did not own specifically identified items of the property which were held in common participatory share ownership, but simply a proportionate participatory share of the entire property.<sup>168</sup> Although the provisions of the civil codes permitted natural persons to hold property by common participatory share ownership, it was traditionally used in ownership relations between collective farms, cooperatives and other social organisations. Common participatory share ownership was always derivative upon the particular "form of ownership" which regulated the underlying relationship between the owners and their common property. As has been noted, the identity of the owners, and hence the relevant form of ownership, would limit the possible objects that could be held in common participatory share ownership in any particular case.

The possession, use and disposition of property in common participatory share ownership was governed by the contract made between the "participants". Expenses relating to the property were divided between the participants in proportion to their participatory shares. Each participant had the right to alienate their participatory share. However, existing participants had pre-emption rights with respect to the participatory share of any selling participant at the sale price or, as applicable, the auction bid. The selling participant had to notify in writing the other participants of its intention to sell, the agreed price and other conditions of sale; and the other participants had 10 days from the communication of the offer to accept.

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<sup>164</sup> RSFSR CC, chapter 12.

<sup>165</sup> 1961 FPCivL, article 26. On this distinction, see M.G.Markova, *Ponyatie i Soderzhanie Prava Obshchei Sobstvennosti* in *Ocherki po Grazhdanskomu Pravu* (Izdatel'stvo Leningradskogo Universiteta:1957), p.91.

<sup>166</sup> See, *supra* n.79, p.82.

<sup>167</sup> *Ibid.*

<sup>168</sup> *Supra* n.41 (1982), p.295.



In addition to the right to alienate their participatory shares, participants also had the right to require the separation of their participatory shares. In the event that the contract between the owners did not provide for this right of separation, it could be sought by judicial process. Furthermore, creditors could apply to the court for the separation of a participatory share. On a request for separation, if the property was fungible and divisible, the participatory share could simply be removed. If it was not divisible, then the entire property could be sold for cash and the cash could be distributed. This could only take place with the consent of all the other owners. If such consent was not obtained, a cash evaluation of the participatory share had to be made and paid over to the separating participatory shareholder. In the event of a dispute, there was the right to take judicial proceedings.<sup>169</sup>



### 3. MODEL 1 - THE CONFIRMATION ENTERPRISE: SOVIET STATE ENTERPRISES AND ASSOCIATIONS

*"The legal entities of the soviet government are in fact sham entities and their mutual contracts are sham contracts. The soviet quasi corporations lack that sufficient freedom of disposal over their property which is the economic background of true corporate status. The property handled by them is not in fact their property but the property of one single owner - the soviet State. Likewise their mutual contracts, being controlled by the general plan and various directives from top agencies, do not express the free will and individual initiatives of the executives of the quasi corporations."*

Vladimir Gsovski

Gsovski correctly pointed out that the Soviet state enterprises were very different from their counterparts operating within the relative freedom of a market economy. But this did not mean that they were "sham entities" but merely that they were creatures of a different order, of a different economy, and now, of a different time... In this Chapter it will be argued that the former socialist state industrial organisations, existing within the Soviet economy in 1985 on the eve of *perestroika*, are best conceptualised within the framework of what has been called the "model of confirmation", as well as by reference to the concept of the unitary state, and in particular the state ownership of the means of production and state planning. By reconceptualising the law of these industrial organisations within the confirmation model, it is hoped to highlight and explain some of their distinct functional and structural characteristics and to present an alternative understanding of their legal regulation which is today still largely derived only from within the tradition of mainstream Soviet law. Furthermore, the confirmation model attempts to analyse the unique role of the state in the creation, ownership and governance of its enterprises; a role that changed throughout the late 1980s, and through



such changes, gave rise to "new" forms of industrial organisation introduced into the Soviet economy after 1987.

The management of the Soviet economy during the period 1918-1920 was characterised by various policy initiatives which Silvana Malle referred to as "an unstable framework for management, which went through three stages: workers' control, state control, party control."<sup>170</sup> Despite early attempts at wholesale nationalisation during that time,<sup>171</sup> it gradually became accepted that some form of goods-money relations would have to play a part within the Soviet economy through state-owned juridical persons. As Lenin famously stated in his report on the New Economic Policy in October 1921, "we must learn to trade".<sup>172</sup> The principle of industrial organisations separated from the central state budget was set out in a series of decrees during the early 1920s,<sup>173</sup> and was confirmed in article 19 of the 1922 RSFSR Civil Code which provided that "state enterprises and their associations transferred to *khozraschet*, and not financed on the basis of the budget, shall enter into [civil law] turnover as autonomous juridical persons and shall not be connected to the Treasury", thereby linking juridical status with *khozraschet*.

Due to their legal status as subjects of civil law separated from the state itself with a separate balance sheet, these state-owned industrial organisations had by definition some degree of legal autonomy over their activities. However, unlike the collective farms where the "personal" interests of the members were required (at least formally) to be taken into account by legislation, the only factor that would determine the level of autonomy of the industrial organisations was the state itself in accordance with its macro-economic policy. As a practical matter, the degree of control ceded by the state to the management of its juridical persons varied over time. Indeed, as official state policy with regard to control and the organisation of the economy changed, so did the structure and size of these industrial organisations. During times of centralisation, industrial organisations were usually consolidated into vertically and horizontally integrated associations or trusts, thereby simplifying the spheres and numbers of economic units and facilitating central management. Conversely, during times of decentralisation, such associations or trusts were generally broken down into constituent

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<sup>170</sup> Supra n.50, p.89.

<sup>171</sup> Supra n.6 (1947), pp.20-27.

<sup>172</sup> Quoted in Olympiad S. Ioffe and Peter B. Maggs, *Soviet Law in Theory and Practice* (Oceana Publications, Inc.:1983), p.137.

<sup>173</sup> Supra n.56 and 57.



enterprises, which led to a more diversified industrial management structure leaving more room for individual initiative. This "cyclical development on the basis of an alternation of opposite reforms - from centralisation to decentralisation and then back to centralisation", Ioffe and Maggs described as "an objective law of economic development in the USSR".<sup>174</sup> Therefore, although the law of the early Soviet industrial organisations was complex and characterised by a number of different policy initiatives, two distinct generic organisational forms emerged: (i) the trust or association (large-scale integrated industrial organisations); and (ii) the enterprise (smaller-scale industrial organisations operating on the basis of more discrete economic functions).

**Trusts** State trusts had their origins in the desire to centrally manage industry during the years of war communism. However, it was during the NEP years of the 1920s that their role and numbers significantly increased. They were originally formed through *ad hoc* legislation,<sup>175</sup> and then through the enactment of various dekrets on state trusts in 1923.<sup>176</sup> The trust, as conceived in the early 1920s, was a juridical person in its own right combining a number of enterprises within its umbrella structure. The 1922 RSFSR Civil Code did not refer to "trusts" explicitly but only to "state enterprises and their associations";<sup>177</sup> however the status of the trust was soon clarified by the adoption of the 1923 Trusts Dekret which in article 1 provided that the trust "shall operate on the principles of commercial accountability with the purpose of deriving profit". In addition, although the state was the owner of the trust and indeed of all of its property, the state was expressed not to be responsible for the debts of the trust and *vice versa*.

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<sup>174</sup> Supra n.137, p.7. They argued that a properly functioning economy must allow for a level of decentralised economy activity. However, the Soviet political system was predicated upon "unlimited political power of the ruling summit" and therefore "the permanent attempts to find a way out of this vicious circle by the Soviet leadership have always necessitated manouvering between centralization and economic decentralization" (ibid, p.2, 6). Harold Berman in reply in his article "The Possibilities and Limits of Soviet Economic Reform" argued that the underlying factors may have been more complex (Olimpiad S. Ioffe and Mark W. Janis (eds.), *Soviet Law and Economy* (Martinus Nijhoff Publishers:1987), p.29).

<sup>175</sup> Venediktov noted that by the end of 1921 there were 430 trusts formed containing 4,144 enterprises with 977,000 workers (A.V.Venediktov, *Organizatsiya Gosudarstvennoi Promyshlennosti v SSSR, Tom II* (Izdatel'stvo Leningradskogo Universiteta:1961), p.56).

<sup>176</sup> Including, the General Model Statute on Associations (Trusts) and Explanatory Note of 12 September 1922; the 1923 Trusts Dekret; and the Dekret of 17 July 1923 regulating those located in local agencies of state administration (ibid, pp.57-58, 63). Venediktov referred to these trusts as "trusts of a new type" to distinguish them from the various forms of association, also called trusts, created during the period 1918-1920 but which operated on the basis of Treasury finance (ibid, p.9, footnote 10).

<sup>177</sup> 1922 RSFSR Civil Code, article 19.



By 1927 industrialisation had become the central plank of Soviet policy and hence increasing attention was paid to maximising efficiencies and production.<sup>178</sup> As such the organisation of industry as a whole was re-examined. In this context, the relationship between planning and centralisation was long debated and it was considered necessary to simplify and concentrate the administrative organs of the economy as well as to decentralise operational management. This resulted in administrative reform of Vesenkha, the delegation of management to republican and local authorities, and increasing the rights of the trusts with the adoption in 1927 of a new Trusts Dekret.<sup>179</sup> The 1927 Trusts Dekret contained no references to "profit" and although it devolved certain activities, it also stressed the subordination of the autonomous operation of the trusts to the requirements of the state plan; and indeed over the next two and a half years the autonomy of the trust gradually became restricted due to the expansion of the authority of Vesenkha.<sup>180</sup>

*Trust Enterprises and Autonomous Enterprises* The history of the "enterprise" was closely linked to that of the trust and under early Soviet legislation its precise legal relationship with the trust was often difficult to discern. Braginsky explained the development of the enterprise as follows: While the 1923 Trusts Dekret contemplated the existence of "trust enterprises" existing within the trust framework ("*trestirovannye predpriyatiya*"), they were neither given separate juridical nor economic status. However, the Dekret also contemplated separate "autonomous enterprises" ("*avtonomnye predpriyatiya*") that operated alongside trusts with identical rights, and in contrast to the trust enterprises, were juridical persons. The trust enterprise eventually was given the status of a juridical person in its own right. Under section IV of the 1927 Trusts Dekret they were transferred to operating on the basis of internal *khozraschet* with a separate balance sheet and one-man management thereby ensuring a degree of economic autonomy from the operations of the trust as a whole. This expression of decentralisation continued with the decree of 5 December 1929 "On the Reorganisation of the Management of Industry" providing for "the enterprise as the basic link in the management of industry".<sup>181</sup> It was shortly afterwards, by a decision of the Council of Labour and Defence on 23 July 1931, that the trust enterprise was given the remaining features of juridical

<sup>178</sup> See, P.I.Lyashchenko, *Istoriya Narodnogo Khozyaistva SSSR, Tom III (Sotsializm)* (Gosudarstvennoe Izdatel'stvo Politicheskoi Literatury:1956), pp.262-274.

<sup>179</sup> Supra n.175, p.373 and 378.

<sup>180</sup> As Zaleski explained: "the role of the trust [in 1923] as an autonomous, market-orientated, and profit-operated economic agency became increasingly compromised" (Eugene Zaleski, *Stalinist Planning for Economic Growth 1933-1952* (The University of North Carolina Press:1980), p.28).

<sup>181</sup> O Reorganizatsii Upravleniya Promyshlennost'yu, *Resheniya Partii i Pravitel'stva po Khozyaistvennym Voprosam, Tom 2* (supra n.51, p.136.



personality, in particular that the circulating assets allocated to it could only be withdrawn in limited circumstances.<sup>182</sup>

***Syndicates and Associations*** The significance of the trust in the Soviet economy was gradually diminished by the growth of "syndicates" in the late 1920s. In response to the crisis in the state industrial sector following the commencement of NEP, Lenin sanctioned the formation of syndicates by groups of trusts in a particular sector. A syndicate would monopolise the marketing of all products by those trusts in that sector in an attempt to increase bargaining strength at a time when market forces tended towards depressing prices. From March 1922,

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<sup>182</sup> Mikhail Braginsky, *The Soviet State as a Subject of Civil Law* (Progress Publishers:1988), p.11 *et seq.* The author has not been able to verify this account from the legislation that was available to him. In particular, the author could not identify the use of the terms "trust enterprises" and "autonomous enterprises" directly in the trusts dekrets and believes Braginsky borrowed this terminology from concepts used by Venediktov and from terminology in other subordinate legislation (*supra* n.175, p.72, 75).

The 1923 Trusts Dekret defined state trusts as "state production enterprises to which the state grants autonomy in the production of its operations...and which shall operate on the basis of commercial accountability with the purpose of attracting profit" (article 1) and provided that "each trust shall be a single enterprise within which shall be several production subdivisions ("*edinitis*") (establishments such as: factories, plants, businesses, divisions, shops etc) listed in its charter. Explanatory note: this dekret may also be applied to enterprises who have within their composition only one production subdivision" (article 3). Thus the 1923 Trusts Dekret implied that state production enterprises combined to form a trust; that state production enterprises existed outside the framework of the trust, however it *did not* use the term "autonomous enterprises" to describe them. Furthermore, it *did not* provide that other enterprises were located within the trust and did not use the term "trust enterprises": there were simply "subdivisions". Perhaps this is what Braginsky meant by the term "trust enterprises". Subordinate legislation did however refer to the concept of enterprises within the trust framework. For example, the "Model Statute on Production Enterprises within the composition of a Trust" adopted by an instruction of Vsenkha on 4 October 1927 referred to subdivisions as capable of existing as enterprises (article 1).

The 1927 Trusts Dekret specifically referred to "*production enterprises*" or "*enterprises*" within the trust (articles 25 and 32), and not simply as subdivisions. As Braginsky correctly noted, they were not explicitly given the status of a juridical person; however the 1927 Trusts Dekret did not specifically state that they were to operate on the principles of *khozraschet* (although article 1 of the Model Statute did state this and Venediktov derived this attribute as a consequence of their other characteristics as set out in the dekret (*supra* n.175, p.271)).

The author has not been able to locate a copy of the decision of the Council of Labour and Defence on 23 July 1931, but neither the Model Statute nor the decree of 5 December 1929 referred to the enterprises within the trust as juridical persons. However a commentary to the civil code published in 1928 noted a judicial interpretation dating to 1924 that considered a factory operating on the basis of *khozraschet* within a trust as a separate juridical person (*Grazhdanskii Kodeks s Postateino-Sistematizirovannymi Materialami* (Yuridicheskoe Izdatel'stvo NKYu RSFSR:1928), pp.100-101).

The increasing role of the enterprise after June 1931 does however accord with the economic history of that year that witnessed Stalin's call for the breaking up of associations on 23 June 1931 in his famous speech, "The New Situation - New Tasks for Economic Construction" which set out the new conditions for industrialisation (13 Stalin 51, at p.79).

A textbook on civil law published in 1950 summarised the position by stating that "the trust enterprise had not been officially named anywhere as a juridical person although legislation and court and arbitrazh practice consider it an autonomous subject of law" (*supra* n.27 (1950), p.170).



leading industries united to create these syndicates. By 1924 the syndicates had become so prevalent that a tension developed between the trusts and the syndicates, the latter ever seeking increased control over the marketing, sale and pricing of production. As the syndicates achieved greater importance in the organisation of production and internal trade, they became the logical institution to be used by the state in the industrialisation drive based on state planning that emerged after the 14<sup>th</sup> Party Congress in 1925. During the years to 1929 the place of the trust in the planned economy became squeezed between the development of the power of the glavki within Vesenkha on the one hand, and the syndicates on the other. A new statute on the syndicates was adopted in February 1928 and by that time they controlled entire sectors of production, issuing compulsory orders to the trusts.<sup>183</sup> In light of the promulgation of the 5 year plan, the organisation of industry was formally restructured pursuant to a decree of 5 December 1929,<sup>184</sup> which specified the "enterprise" as the basic link. In addition it reorganised the syndicates into "associations" of enterprises ("*ob''edinenie predpriyatii*"),<sup>185</sup> within which were located enterprises alone, or a combination of trusts and enterprises.<sup>186</sup> While the rights of the enterprise were increased, the associations were given power over their management and sales.

Therefore, from the earliest days of Soviet management of the economy, tensions existed between the association and the enterprise; between centralised management of the economy through large-scale monolithic industrial organisations and decentralised control through increased local discretions; and perhaps ultimately, between the principles of planning and *khozraschet*.<sup>187</sup> Prevailing legislation invariably provided for both forms of organisation, the association and the enterprise; however, their importance and the detail of the applicable legislation was dependent upon the official state macro-economic policy of the time.

Various policy initiatives were carried out in the period to 1964 and the accession of Brezhnev. Most notably, in "1957 there occurred the largest restructuring of the system of

<sup>183</sup> E.H.Carr & R.W.Davies, *Foundations of a Planned Economy, Volume One (I)* (1969, reprinted Macmillan:1978), p.376.

<sup>184</sup> Supra n.181.

<sup>185</sup> Associations had also existed in their own right since the early 1920s and hence were mentioned in article 19 of the 1922 RSFSR Civil Code; however their role developed most significantly after the 1929 restructuring of the industrial economy.

<sup>186</sup> The development of the enterprise and trust separately from the syndicate or association gave rise to the so called "double link" system of administration (state agency-enterprise) and the "treble link" (state agency-trust-enterprise) (see also supra n.175, p.72). Later the "quadruple link" was introduced in certain sectors of the economy such as coal and oil production, (state agency-combine-trust-enterprise) (S.S.Studenkin, *Sovetskoe Administrativnoe Pravo* (Gosudarstvennoe Izdatel'stvo Politicheskoi Literatury:1954), p.136).

<sup>187</sup> Supra n.57 (1948), pp.484-494.



central state agencies" when the management of industry and production was transferred to the soviets of the national economy.<sup>188</sup> As part of this decentralisation, the management of the economy was reorganised on the basis of territory governed by the soviets, as opposed to on the basis of branches.<sup>189</sup>

The legislation on the eve of *perestroika* contemplated both of these two different types of industrial organisation; however the law of the 1920s and 1930s had been replaced by two further periods of legislative reform: one in the late 1960s which established the legislation on "enterprises", and the second in the early 1970s which established the legislation on "production associations".

***State Socialist Enterprises*** Despite the reforms in the administration of the economy in 1957, the operation of the economy remained highly regulated and, as Ioffe and Maggs noted, the "extremely centralised management of the economy, established by Stalin and actually left unchanged by Khrushchev, led to persistent economic stagnation, which presaged inevitable disaster, if some drastic steps were not taken".<sup>190</sup> Pursuant to the resolutions of the 1965 September Plenum of the Communist Party, there began a twin policy of increasing centralisation of the administration of the economy by restoring centralised industrial ministries, while at the same time decreasing their right to control the day-to-day activities of enterprises within their competence.<sup>191</sup> The aim, once again, was to make the entire planned economy more flexible and responsive to demand.<sup>192</sup> This was furthered through the adoption of two decrees, first, on the Perfecting of Planning and Strengthening of the Economic Stimulation of Industrial Production in October 1965, and then through the adoption of a General Statute on Ministries in USSR in 1967.<sup>193</sup>

The reforms of the mid-1960s saw the individual de-centralised state enterprises as the key to re-invigorating the Soviet economy. The centrepiece of the reforms was the Enterprise Statute

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<sup>188</sup> Supra n.41 (1982), p.34-35.

<sup>189</sup> V.A.Vlasov, SS.Studenkin, *Sovetskoe Administrativnoe Pravo* (Gosyurizdat:1959), pp.321-326.

<sup>190</sup> Supra n.172, p.140.

<sup>191</sup> See, Alec Nove, *An Economic History of the USSR 1917-1991* (Penguin Books:1992), p.378. This decentralising trend was noted in the new 1961 Communist Party Programme - "The economic autonomy and rights of local agencies and enterprises will continue to expand within the framework of the single national economic plan. Plans and recommendations made at a lower level beginning with enterprises shall have an increasing role to play in planning." (supra n.58, p.262).

<sup>192</sup> Supra n.6 (1985), pp.364-5.

<sup>193</sup> O Sovershenstvovanii Planirovaniya i Usilenii Ekonomicheskogo Stimulirovaniya Promyshlennogo Proizvodstva, (1965) 4 *SDZ SSSR* 5; Obshchee Polozhenie o Ministerstvakh SSSR, (1967) 25 *SDZ SSSR* 99.



adopted by a decree of the Cabinet of Ministers in 1965.<sup>194</sup> It was the first time during the Soviet period that a specific legislative statute was adopted dedicated solely to the regulation and juridical status of the enterprise (as opposed to the trust, syndicate or association). In line with the policy of decentralisation, article 1 provided that the enterprise was to be "the basic link in the national economy of the USSR". The Enterprise Statute aimed at devolving broad control to the management in a number of areas including price setting, determining production output and hiring and dismissing its employees. Furthermore, plans became more generic and thereby seemed to increase the formal opportunity for "contracting" and exercising individual discretions.

*Production and Industrial Associations* Predictably, this decentralising trend did not last long. The administrative structure of the Soviet economy was again reorganised as soon as 1973.<sup>195</sup> Once again consolidation and economies of scale were stressed as theory harked back to the centralisation of the economy in the late 1920s with its vast state trusts and syndicates. Ioffe and Maggs attributed this further change in policy to the rapid effect that the reforms of 1965 had on consumer demand which "threatened with immediate collapse the always feeble system of supply" coupled with the failure of the simplification of planning.<sup>196</sup> In the tradition of the principles set out in the decree of December 1929, state enterprises were reorganised into "production associations", which in turn were sometimes subordinated to new "industrial associations".<sup>197</sup> These new industrial and production associations were created respectively pursuant to Decree 139 "On Some Measures on the Further Perfecting of the Management of Industry",<sup>198</sup> and Decree 140 confirming the Industrial Association Statute.

Article 2 of Decree 139 provided for two types of vertical relationships in the Soviet economy: the double link (Ministries (all-union or republican) - production association

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<sup>194</sup> On the substantive legal reforms of the late 1960s, with particular reference to Kazakhstan, see *Khozyaistvennaya Reforma i Prava Predpriyatii, Tom 1 i 2* (Izdatel'stvo Kazakhstan:1969, 1971). See, generally, Alec Nove, *The Soviet Economy, An Introduction* (George Allen & Unwin Ltd:1968), pp.31-44.

<sup>195</sup> Ioffe has argued that the process of recentralisation was even more rapid and in practice began within a year or so after the 1965 reforms (see O.S.Ioffe, *Law and Economy in the USSR*, (1982) 95 *Harv.L.Rev.* 1591, pp.1621-23).

<sup>196</sup> *Supra* n.172, p.140.

<sup>197</sup> On the context of these reforms within the prevailing Soviet and western theories of management, see William J. Conyngham, *The Modernization of Soviet Industrial Management* (Cambridge University Press:1982).

<sup>198</sup> O Nekotorykh Meropriyatiyakh po Dal'neishemu Sovershenstvovaniyu Upravleniya Promyshlennost'yu, (1973) 25 *SDZ SSSR* 122.



(combine) or enterprise) and the treble link (Ministries (all-union or republican) - industrial association - production association (combine) or enterprise).<sup>199</sup>

Industrial associations created by Decree 140 were to make up a "unified production-economic complex" being more administrative in their nature than the production associations.<sup>200</sup> They were juridical persons with their own property and management organs. Enterprises operating on the basis of the Enterprise Statute, and other organisations operating on a different basis, were located within their structure.<sup>201</sup>

A year later the Production Association Statute was adopted.<sup>202</sup> In accordance with article 1, production associations were to be the "basic (primary) link of industry".<sup>203</sup> Throughout the 1970s many smaller enterprises were reorganised and merged into production associations thereby losing their separate juridical personality. However some enterprises, operating on the basis of the Enterprise Statute and retaining juridical personality, remained in existence after this restructuring of the economy either directly subordinate to a Ministry (the "double-link") or within a production association.<sup>204</sup>

By 1985, the Enterprise Statute, the Industrial Association Statute and the Production Association Statute were still the basic statutory enactments on Soviet industrial organisations operating on the basis of *khozraschet*. In economic terms the emphasis on associations gradually waned. In volume 12 of the SDZ SSSR on civil law published in 1976, the Enterprise Statute was cited before the Production Association Statute, which in turn was cited before the Industrial Association Statute.<sup>205</sup> Despite the initiatives in the early 1970s, by 1979,

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<sup>199</sup> Supra n.60 (1973), p.339. This division was based on the link system of management developed in the 1930s (supra n.186).

<sup>200</sup> Industrial Association Statute, article 1.

<sup>201</sup> Industrial Association Statute, article 7. Supra n.41 (1986), p.140.

<sup>202</sup> Similar statutes were passed to regulate other areas of the economy such as the Polozhenie o Nauchno-Proizvodstvennom Ob''edinenii, (1975) 9(II) SDZ SSSR 330.

<sup>203</sup> Cf. article 1 of the Enterprise Statute which remained in force and provided that enterprises would be "the basic link in the national economy".

<sup>204</sup> Article 1 of the Production Association Statute set out the general principle that enterprises "within" production associations would not be juridical persons and that the Enterprise Statute would not apply to them. However, article 6 provided an exception that, by decision of the appropriate Ministry or Council of Ministers, enterprises that were juridical persons could operate within associations. Production associations containing such enterprises operating on the basis of the Enterprise Statute within them were termed "associations of a mixed type" (see V.V.Laptev, Pravovye Voprosy Sovershenstvovaniya Rukovodstva Promyshlennost'yu in *Nauchno-Tekhnicheskaya Revolyutsiya, Upravlenie i Pravo* (Niimash:1975), p.88). On the relationship between associations and enterprises "within" them, see infra Section 6.5.1.

<sup>205</sup> 12 SDZ SSSR 94, 103, 109. The order in which provisions appeared in Soviet statutes, or sections appeared in textbooks, was generally an indication of their relevant importance. Furthermore the SDZ



in purely economic terms, production associations accounted for just less than half of the output of all industrial production in the Soviet economy.<sup>206</sup> By 1985/86 official policy formally shifted to recognise this change in emphasis, and the restructuring of the national economy was declared to be based on state enterprises.<sup>207</sup> A textbook on Soviet civil law published in 1986 even incorrectly referred to "enterprises - the basic (primary) link in the national economy of the USSR" thereby giving enterprises a designation that was reserved for productions associations.<sup>208</sup> After an extensive section on the operation of enterprises, the textbook then referred to production associations almost as a derivative form of enterprise: "in the organisational structure of the economy there also operates production associations (combines) in the same place as the enterprises".<sup>209</sup> Of course, as originally conceived in the early 1970s, the situation was to be the reverse: the production association was to be the over-arching economic organisation within which enterprises would be located.

As has been outlined, in *economic* terms, the difference between the production association and the enterprise reflected primarily the difference between two competing theories of industrial organisation and management. The one, which gave rise to the production association, trust or syndicate, stressed the centralisation of units of production, horizontal and vertical integration, and simplification of branches within the national economy. The other, which gave rise to the enterprise, stressed de-centralisation and flexibility within units of production. Despite this difference in economic approach, from a *legal* point of view, the state enterprises and the production associations were remarkably similar. Juridical personality and *khozraschet*, together with the management organs, were simply abstracted to a consolidated entity: from the state enterprise to the production association.<sup>210</sup>

Due to their increasing importance in economic terms throughout the late 1970s and 1980s, and given their legal similarity with the production association, this Chapter focuses on the

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SSSR contained an extensive footnote covering three pages which set out the extent to which the Enterprise Statute continued to apply to industrial organisations in various sectors of the national economy (12 *SDZ SSSR* 94-96, footnote 1).

<sup>206</sup> See article, *Proizvodstvennye Ob''edineniya*, *Pravda* (3 July 1979), p.1.

<sup>207</sup> See, Report of Ryzhkov to the Politburo "On the Restructuring of the Administration of the National Economy to an Advanced Stage of Economic Development of the Country" (*Izvestiya* (29 June 1987), pp.1-4). The nature of these "new" state enterprises are analysed within the participation model (infra Section 6.3).

<sup>208</sup> *Supra* n.41 (1986), p.135, 137-8. The term "(primary) link" was only used in article 1 of the Production Association Statute and not article 1 of the Enterprise Statute.

<sup>209</sup> *Ibid.*

<sup>210</sup> As Butler noted: "the functions of enterprise independence were principally elevated to the production association or even the industrial association" (*supra* n.21, p.251).



state enterprise in the elaboration of the confirmation model. However, the framework of the confirmation model is equally applicable to the production association, and the peculiarities and provisions of the Production Association Statute are referred to as relevant.<sup>211</sup>

### 3.1 The Role of the Soviet State and the Confirmation Model - General Principles

Irrespective of any specific macro-economic trend or initiative of the Soviet regime at any particular time, it shall be argued that there was always a constant and distinct role that the state enterprise and production association fulfilled within the operation of the Soviet economy as a whole. And it is this particular role that perhaps best defines the nature of these industrial organisations and is the basis for the elaboration of the confirmation model.

In accordance with Marxist-Leninist ideology, almost from its inception the Soviet state was built upon a dictatorship by the Communist Party and a rapid extension of direct state ownership over the industrial economy. This situation necessitated the development of a state policy that not only regulated the macro-economy, but also that determined the matrix of all industrial activity at the level of the micro-economy, given that the means of production were entirely in the hands of a single person - the state.

During the early years of Soviet power, it was unclear as to how these two functions could have been accommodated within a single state structure and ideology. However, as described above, by the late 1920s a policy was settled upon that was to endure, almost intact, through to 1991; and it shall be argued that this involved the Soviet state acting in four quite distinct capacities.

*State as Legal and Economic Sovereign* The Soviet state was not only the basis for the Hartian "rule of recognition" in the Soviet legal system, it was also the owner of the entire economy. This enabled it, as "legal sovereign", to adopt legislation that was binding upon all persons and, as "economic sovereign" (or feudal overlord), to promulgate plans and issue administrative instructions, that were binding on all persons owned by, or using assets that were owned by, the state.

These two capacities enabled the state to adopt legislation, devise plans and issue instructions in the running of the macro economy. However, the decision to run the economy on the basis of an economic plan still left open the question as to the nature of the matrix of the micro-economy and thereby the nature of industrial activity - ie who would be the addressees of the

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<sup>211</sup> In fact, as an illustration of their legal similitude, the State Enterprise Law of 1987 included both the production association and state enterprise within a single legal framework. This is considered in more detail, *infra* Section 6.1.2 *et seq.*



planned instructions? This was particularly problematic in a state where entrepreneurial activity was illegal,<sup>212</sup> where the scope of property that could be held in personal ownership was severely limited,<sup>213</sup> and where the vast majority of the wealth in the economy, the means of production, was located in the ownership of the state.

The early nationalisation decrees side-stepped this issue. For example, one of the first nationalisation decrees adopted on 28 June 1918, relating to nationalising important areas of industry, provided that ownership was to be nationalised, but that the management structure was explicitly expressed to be unaffected by this change in ownership until Vesenkha had issued specific instructions to specific enterprises.<sup>214</sup> Hence while nationalisation was vigorously pursued, the nature of the matrix of the organisation of the micro-economy was deferred until an appropriate framework could be developed.

A possible solution would have been for state agencies themselves to have been the addressees of the plan and carry out the day-to-day running of the economy. This would probably have resulted in the state underwriting their balance sheets, and an element of civil law relations being ceded to the ambit of administrative law. No doubt this would have been the most attractive method of organising the matrix of the micro-economy and the nature of industrial activity because it rather crudely preserved the role of the dictator state and state ownership while at the same time would have been capable of accommodating the notion of state planning. Ioffe noted that such centralisation would have been "most appropriate to the demands of unrestricted political power";<sup>215</sup> and indeed during the period of war communism, the Soviet regime flirted with the notion of a matrix for the micro-economy based on institutions of state administration.<sup>216</sup>

However, as a matter of pure economics, the "administrative state" as attempted during the period of war communism failed and the Soviet regime was therefore forced to contemplate a

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<sup>212</sup> See, for example, 1960 RSFSR CrimC, article 153 on "Private Entrepreneurial Activities and Commercial Middlemen" and article 154 on "Speculation" (see *Kommentarii k Ugolovnomu Kodeksu RSFSR* (Yuridicheskaya Literatura:1984), pp.304-312). The criminal codes of the other republics contained similar provisions.

<sup>213</sup> Supra Section 2.4.3.

<sup>214</sup> Supra n.111 (1967), p.95.

<sup>215</sup> Olimpiad S. Ioffe, *Soviet Law and Soviet Reality* (Martinus Nijhoff Publishers:1985), p.124.

<sup>216</sup> Chamberlin included in his "six principles" of war communism: "the state through its central and local organs took over all the means of production and reduced the sphere of private ownership to the narrowest possible limits"; "state control over the labour of every citizen"; and "extreme centralisation" (William Henry Chamberlin, *The Russian Revolution 1917 -1921, Volume Two* (Macmillan & Co., Limited:1935), pp.97-98).



level of decentralisation.<sup>217</sup> The solution therefore to the question of the nature of the matrix of the micro-economy and the nature of industrial activity was found by "developing" two additional capacities through which the Soviet state could operate, based on the concept of "owner" as opposed to "sovereign". These capacities were particularly apposite in the context of the NEP economy and enabled a "state sector" to be developed in "competition" with the private sector.

***State as Creator-Owner*** The Soviet state founded state trusts, associations, syndicates and enterprises. Despite the fact that they were created by the state and hence remained in state ownership, they were characterised as separate subjects of civil law in their own right with the legal capacity to bear rights and assume obligations. As described by article 19 of the 1922 RSFSR Civil Code, they were "autonomous juridical persons" with responsibility for the obligations that they assumed, separated from that of the administrative state.<sup>218</sup>

The establishment of state enterprises provided an addressee of the plan which was a specialised industrial organisation, a separate subject of civil law, capable of operating and being evaluated as an independent economic unit on the basis of *khozraschet* with a separate balance sheet. This therefore enabled the state to evaluate the performance of each industrial organisation on its own terms, separate from the responsibilities of the state.

***State as Property-Owner*** Having created, as addressees of the plan and the principal actors in the new Soviet Stalin economy, the concept of state-owned juridical persons which were "organs of the national economy and not agencies of state power",<sup>219</sup> a method had to be found by which property could be used by these organisations without prejudicing the principle of state ownership of the means of production. The solution was found in the Soviet law on ownership which contemplated the "allocation" of state-owned property to state-owned juridical persons for their possession, use and disposition but without, in legal doctrinal terms, the transfer of "ownership". Therefore while property in the "operative management" of state-

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<sup>217</sup> The catastrophe of war communism has been widely documented: "...war communism...did not work, because it deprived producers of all possible incentives" (ibid); "The economic consequences of war communism, whose bankruptcy was revealed by these events[:])...a catastrophic decline in industrial production...followed by a virtual breakdown of state or state-controlled distribution...leading to...wild currency inflation...goods famine...a worthless currency...and industrial production brought still nearer to a standstill" (E.H.Carr, *The Bolshevik Revolution 1917-1923, Volume Two* (1952, reprinted Macmillan:1994), p.272); and "war communism...left Russia's economy in shambles...A contemporary Communist economist called the economic collapse a calamity "unparalleled in the history of mankind"... (Richard Pipes, *Russia Under the Bolshevik Regime 1919-1924* (Fontana Press:1995), p.371).

<sup>218</sup> This formulation of the nature of the state trusts was expressed in article 1 of the 1923 Trusts Dekret which provided that "the State treasury shall not be responsible for the debts of trusts".

<sup>219</sup> Explanatory note to article 1 of the 1923 Trusts Dekret.



owned juridical persons appeared on their balance sheets as "belonging" to them,<sup>220</sup> such property remained in state ownership.

The state-owned industrial organisation therefore gave rise to an individual unit that was owned by the state and whose property remained in state-ownership and that acted as the addressee of planned instructions. However, at the same time, it was a legally autonomous civil law person separated from the administrative state and operating on the basis of "its" separate balance sheet. The solution to the question of the nature of the matrix of the micro-economy and the nature of industrial activity through the use of the juridical person in its capacity as an organ of the national economy was ingenious for it did not determine the extent to which any centralising or decentralising policy would prevail, but merely acted as a pivot on which the balance could be adjusted,<sup>221</sup> accommodating within its formulation the trust, the association, the syndicate and the enterprise. Many commentators, both lawyers and economists, have noted the centralisation/decentralisation tension within the Soviet economy, and in the abstract, the role of the Soviet state both in planning and in production.<sup>222</sup>

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<sup>220</sup> The phrase "belonging to" and "allocated to" were used interchangeably in legislation; see for example 1961 FPCivL, article 13 (quoted *infra* Section 3.3 under the heading "Autonomous Property Responsibility").

<sup>221</sup> Ioffe referred to this balance as the "golden mean...based upon the plan and *khozraschet*...The plan represents the centralizing trend...imperative and detailed...[and] *khozraschet*, represents the decentralising trend...legal security and economic freedom...[and the] Soviet leadership insists upon "the correct combination" of plan and *khozraschet*" (supra n.215, p.125-126). On this balance and the Stalin economic settlement, see supra Section 2.2.

<sup>222</sup> Ioffe and Maggs distinguished between the "agencies of planning" and the "agencies of production" (supra n.137, p.105 and 115).

Textbooks on Soviet civil law both within the Soviet Union and outside acknowledged the special status of the Soviet state and indeed most contained a separate chapter on "The Soviet State as the Subject of Civil Rights" which was aimed at explaining the unique status of the Soviet state, as owner of the means of production on the one hand, but not the direct bearer of civil rights on the other. Reference was therefore made to juridical persons and the fact that while property was allocated to them by way of operative management, it remained in the ownership of the state (for example: "The Soviet socialist state is a single owner of all state property" (art 21, 1961 FPCivL)). The principal mass of property belongs to the state and is distributed among state organisations - juridical persons - which manage it on its behalf" (supra n.41 (1986), p.105)).

However despite this debate as to the nature of the Soviet state and the usual explanations of the uniquely socialist nature of state ownership and operative management, it is rare to find in this context an analysis of the nature and rationale of the state industrial organisation itself and the way in which it could be viewed as the tool by which the state in its four capacities could plan the national economy on the basis of some level of decentralised economic activity without compromising the ability to apply, as necessary, continued central control. One allusion to this argument was made by Ioffe and Maggs: "...ownership of the means of production must be used for productive tasks. And since these tasks cannot be accomplished by the state as a political organisation, it has no other way out than to create numerous economic organisations for the aims of production. These organisations must use certain property if they are to produce, and the State must distribute among them sufficient property if it has to be used productively" (supra n.172, p.133). However Ioffe and Maggs were less interested in an analysis of state-owned



However, this Chapter 3 has gone further and has argued that the industrial organisation should be conceptualised as a puppet of the Soviet state whose role was as an adjunct to the planned economy, cast as the addressee of planned instructions and elaborated on the basis of the state acting in four distinct capacities (as legal sovereign, economic sovereign, creator-owner and property-owner). The confirmation model has been developed on the basis of these four faces of the Soviet state and reconceptualises the place and significance of the then prevailing legislation in this light.

Once it was decided to organise the industrial economy on the inter-locking principles of state ownership of the means of production, national planning and state-owned juridical persons, the question of the creation of those juridical persons was little more than a formality and would always be carried out by a state act adopted by the duly empowered state agency in accordance with the current state plan. The notion of corporate, or juridical, status conferred by state act or royal charter has given rise to a number of heuristic theories and models, many developed in terms of a "concession from the state": corporate status being a privilege granted by the state to certain types of association.<sup>223</sup> However the concept of juridical status resulting from a "concession" or "privilege" is singularly inappropriate in the context of a unitary state owning all the means of production and where the possibility of founders petitioning the state for the granting of juridical personality upon their informal contract-based association is chimerical. Rather, by the act of "confirmation" the unitary state itself created enterprises and controlled their activities by acting in the four separate capacities. To this extent Gsovski was right to point out that "the legal entities of the soviet government" bore little resemblance to the juridical persons in market economies. Accordingly, it will be argued that the state enterprise and production association, distinctly Soviet forms of association, are best analysed in terms of, what has been called, "the model of confirmation".

The model of confirmation was derived from an understanding of the separated industrial juridical person as the "addressee" of planned instructions operating within a single state owned unified national economy. The leitmotif of "confirmation" encompasses all of the four capacities of the state, for the state: as legal sovereign confirmed the civil law legislation setting out the legal framework for these industrial organisations; as economic sovereign confirmed the state plan which set out the necessity for their creation and the nature of their operations; as economic sovereign and creator-owner confirmed the decision to create them,

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industrial organisations and more in developing the argument that an element of decentralisation within a functioning economy was inevitable despite a political system unwilling to accommodate such.

<sup>223</sup> Sally Wheeler (ed.), *A Reader on The Law of the Business Enterprise* (Oxford University Press:1994), p.7. The concept of the "concession" and its role in analysing certain types of association is considered in more detail infra Chapter 5.



by order of the relevant state agency; as creator-owner drafted the contents of their charters; as property-owner confirmed the designation of the organisations' property and the allocation of such property to them (as set out in the applicable charter); upon confirmation of the charter by registration, as legal sovereign conferred juridical personality upon the organisations; and finally as economic sovereign and creator-owner would confirm, when it deemed expedient, the decision for any of them to be terminated. Therefore, the model of the confirmation enterprise displays a number of hallmark characteristics:<sup>224</sup>

- (i) creation and termination by diktat as determined by the plan (with few legal procedural requirements);
- (ii) autonomy and separate status as a consequence of juridical personality with solitary property (operating on the basis of *khozraschet*) and with autonomous property responsibility; and
- (iii) a crude governance structure characterised by the unitary state acting in each of its capacities:
  - (a) as creator-owner, responsible for the drafting of a charter that carefully detailed its capacity, and the appointment of the single one-man manager;
  - (b) as property-owner, retaining the right of ownership of the property allocated to the enterprise which was held by way of operative management; and
  - (c) as legal sovereign and as economic sovereign, both in the form of the polity and the party, through legislation, instruction, and the elaboration of the central state plan.

The creation of these confirmation enterprises was a relatively straightforward matter as the state owned all the means of production (and hence all industrial enterprises). There were no legislative or other impediments to their creation. There were no individuals petitioning for the granting of corporate status upon their informal association. The creation of state enterprises had nothing to do with a negotiation between the state and a third party (the so-called "promoters" or "founders"), as described in the various concession theories. Instead, it was the product of simple confirmation based on "objective necessity" as identified in the plan. If the plan so provided, the creation of the state enterprise would be assured. It was simply "confirmed" in the appropriate manner. Similarly, the termination of these enterprises followed the same model. As a result, the law governing the creation and termination of state enterprises was underdeveloped, for it was more a question of pure politics rather than law

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Each are considered in more detail in the following Sections of this Chapter.



that was the overriding determinant: law is only necessary if there is scope for negotiation or application, but less so in the context of simple confirmation.

As aforementioned, the creation of these separate industrial organisations by confirmation necessarily presented a "governance problem". Once created, a Soviet industrial organisation had separate civil law status; was separated from the institutions of the administrative state; had a separate balance sheet (operating on the basis of *khozraschet*), solitary property and autonomous property responsibility. The Soviet state therefore had to find appropriate techniques to allow it, as appropriate, to control and restrict their activities so that while retaining a civil law mask of autonomy, these state-owned industrial organisations could be compelled to act in accordance with the objective requirements of the Soviet state as expressed in the state plan. This was essentially achieved in four ways: a charter that carefully detailed its capacity (coupled with a strong *ultra vires* rule); property without ownership (held by way of operative management); one-man management; and general legal and administrative diktats. This governance regime should not appear strange once it is understood that its design was to regulate an entity that was the product of mere confirmation - a puppet with its own head and costume, but always intended to bow and move, as necessary, in accordance with the movements of the invisible hand of the puppeteer - the Soviet state.

The constitutive documents of the state-owned industrial organisation generally set out the internal framework for its operation. In the Soviet context there were only two "interests": the state and its appointee (the director of the enterprise).<sup>225</sup> This can be contrasted with the constitutive documents of market economy juridical persons which generally have to balance a variety of interests including those of majority shareholders, minority shareholders, directors, creditors, workers etc. The principal constitutive document of the state enterprises, the charter, was above all a control mechanism to ensure that the appointee of the state, the one-man manager, acted strictly in accordance with the purpose for which the state enterprise was created. The purpose clause in the charter was critical for under Soviet civil law a juridical person was only permitted to carry out an activity to the extent it was expressly contemplated in the charter. In the absence of a special permission, an activity was prohibited. Purpose clauses were usually sufficiently precise to ring-fence activities as well as sufficiently vague so as to be open to *ex post facto* interpretation should the state wish to limit further or to broaden further the discretions of its appointee.

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<sup>225</sup> The Soviet ideology of the "all-people's state" explained that not only had class conflict been abolished in the Soviet Union, but also that there was a coincidence of interests between the interests of the state and the interests of the people (see *supra* n.92 *et seq.* and *infra* n.538 *et seq.*).



In addition to specifying the contents of the charter, control over the activities of the confirmation enterprise by the state was also effected through the peculiar nature of the Soviet law on ownership. For while the concept of operative management preserved in ideological terms state ownership of the means of production, it also meant, as a practical matter, that the property "of" a state enterprise was never owned by it. Therefore, the state agency responsible for the creation of a state enterprise and the allocation to it of state property, could designate restrictions on the use of that state property by the state enterprise due to its continuing ownership of that property. As such, in addition to controlling the activities of the state enterprise in the more "traditional" ways as "owner of the organisation" (through the charter and appointment and removal of the management), the state retained control over its activities through being at all times the direct and continuing owner of "its" property.

State control was further achieved by way of the management structure. One-man management allocated power in a single source. This facilitated an efficient framework for the implementation of state policy without committee deliberation or debate, and enabled the entire management of an enterprise to be instructed with relative ease. There was a single owner, the Soviet state, which had one representative, a single director. Political dictatorship was reproduced as economic dictatorship. Orders confirmed from above would be confirmed by the director and implemented by the workers. One-man management also meant one-man accountability and responsibility. Therefore if an enterprise was performing below its targets as set by the plan, there was only one-manager or director that would need to be replaced, thereby further facilitating central control.

There was a final control mechanism at the disposal of the Soviet state which, strictly speaking, fell outside the "governance structure" itself. The Soviet state could use its position as "sovereign" to ensure that its enterprises acted in accordance with its requirements. Therefore, as legal sovereign, the state could have adopted generic or specific legislation of all types, including the Enterprise Statute itself, aimed at compelling the directors of its state enterprises to act in a particular way. Furthermore, as economic (or feudal) sovereign, general plans and planning instructions could have been elaborated by duly empowered state agencies, including Gosplan, and would have been binding on the state enterprises.<sup>226</sup>

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<sup>226</sup> As Ioffe explained, "Perhaps no Soviet enterprise has managed to work even one year in its entire history without suffering economic damage and production arrhythmia due to the abrogation or modification of its production or other plans by planning agencies of various levels" (Olimpiad S. Ioffe, *Soviet Law and the New Economic Experiment* in *supra* n.174, p.13). The 1965 legislative initiatives tried to introduce a mechanism by which planning agencies could be responsible for damage caused to addressees of planned tasks. This was rarely used in practice and was complicated by the edict of Jan 1967 which provided that Ministries had to set up reserve funds from which these compensation payments would be made but that



Finally, in addition to the formal law-making controls that were available as sovereign, the Soviet state (in the widest sense of the term) also exercised control over the activities of its industrial organisations through the "shadow agencies" of the Communist Party. As Ioffe and Maggs noted, "direct subordination means nothing else than subordination of economic organizations to the Communist Party's instructions. In order to keep a close watch on the Soviet economy, the Party maintains its own economic bureaucracy, which parallels that of the government...[in fact]...all...hirings and firings [of general directors] are predetermined by competent Party agencies."<sup>227</sup>

In short, the development of this multi-faceted Soviet state presented a number of overlapping ways that the state and Party could have ensured compliance by the confirmation enterprise with its instructions, and there was therefore no necessity to identify the specific mechanism that was being adopted in any individual case. There was certainly no need to develop in particular a governance framework based solely on the role of the state as creator-owner with a developed understanding of the concept of an ownership interest of the state enterprise and of the nature of the rights and obligations arising in connection with such interest. As a result, the logic of the confirmation model provided an inappropriate foundation or starting point for the development of industrial organisations based on fragmented ownership and the attraction of equity capital.

The confirmation enterprise is perhaps a uniquely Soviet phenomenon and lends support to the view that the Soviet legal system spawned a very distinct set of legal principles and creations.<sup>228</sup> The concept of state control over the national economy and ownership of the means of production (by way of the plan and state ownership) gave rise to an enterprise that could be created and liquidated by mere confirmation, that can be conceptualised with reference to the civil law concept of juridical personality and whose operations were controlled by a peculiar system of governance based on *vires*, operative management and one-man management, coupled with pervasive influence of the Soviet polity as legal and economic sovereign and through the party.

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all disbursements would be at the discretion of the appropriate ministry (thereby leaving enterprises with the right to claim but without the right to be compensated).

<sup>227</sup> Supra n.172, p.148 *et seq*, 151. In another work, Ioffe described the "unwritten part of civil law" as consisting "by and large, of oral Party directives" which "has superior force over published legal norms" (supra n.123 (1988), p.13).

<sup>228</sup> See supra Section 2.2.



### 3.2 Formation, Reorganisation and Liquidation by Confirmation

Juridical personality throughout pre-revolutionary Russian legal history was perhaps best regarded in terms of a grant from the state.<sup>229</sup> In contrast with "general incorporation statutes" where the establishment of juridical personality is a right (provided that the certain general procedural formalities are followed),<sup>230</sup> juridical personality conferred by an individual state act necessitates a specific exercise of discretion by the state (or its sub-division) on a case-by-case basis. As discussed, under Soviet law, the decision to create industrial organisations was taken within the framework of the state plan and the requirements of the national economy. Where the objective needs of the economy required the creation of an enterprise in a particular branch of the economy to fulfil a specific function then that enterprise would be created by the appropriate state agency as a matter of simple confirmation.

The 1961 FPCivL did not provide any specific method or procedure for the establishment of juridical persons (including state enterprises and associations) and the civil codes contained the broad principle that the formation of juridical persons should be carried out "in the procedure established by legislation" of the USSR and the relevant union republic.<sup>231</sup> Soviet legal doctrine however contemplated three procedures ("*tri poryadka*") for the formation of juridical persons in general: (i) by order ("*rasporyaditel'nyi*"); (ii) by permission ("*razreshitel'nyi*"); and (iii) normatively by initiative ("*normativno-yavochnyi*").<sup>232</sup>

In theory, the particular procedure that was applicable depended upon the identity of the creator of the juridical person and the nature of the resulting juridical person.<sup>233</sup> Therefore in doctrinal terms: the first procedure was reserved for state enterprises created by order of the duly empowered state agency;<sup>234</sup> the second procedure was to be used where a voluntary association sought permission for juridical status; and the third procedure covered the situation where citizens had created juridical persons by their own initiative (and was particularly associated with the "spontaneous" formation of collective farms). Ioffe as a practical matter

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<sup>229</sup> On the creation of pre-revolutionary joint-stock societies, see L.E.Shepelev, *Aktsionernye Kompanii v Rossii* (Izdatel'stvo Nauka:1973), pp.20-21.

<sup>230</sup> Examples of general incorporation statutes include the English Companies Act 1985 (as amended) and the General Corporation Law of the State of Delaware contained in Title 8, Chapter 1 of the Delaware Code of 1951 (as amended).

<sup>231</sup> See, for example, RSFSR CC, article 27.

<sup>232</sup> Supra n.27 (1950), p.151.

<sup>233</sup> Supra n.41 (1986), p.125-126.

<sup>234</sup> While some civil codes simply referred to formation in accordance with the procedures established by legislation, others such as the Kazakh civil code went further and referred specifically to creation of "state juridical persons" by "order of the duly empowered state agency" (Kaz CC, article 26).



rejected the notion of collective farms as having been created "voluntarily",<sup>235</sup> and concluded that "the system of commands, although formally compatible only with state organisations, is in fact the universal system for the creation of juridical persons of all types in the USSR".<sup>236</sup> This view was broadly (albeit differently) confirmed by Soviet civil law textbooks which stressed the guiding influence of the state in the creation of all juridical persons and thus concluded generically that "a juridical person may not arise other than from state power. The state regulates and controls the process of arising of the juridical person in this or any other form."<sup>237</sup>

There was only one article of the Enterprise Statute that governed the question of formation and it reflected the general position outlined above providing that "an enterprise shall be formed by order (decision) of a superior agency in accordance with legislation of the USSR or union republic".<sup>238</sup> The superior state agency itself was not identified but, as set out in subordinate legislation, it was usually the relevant ministry responsible for the specific branch of the economy.<sup>239</sup> The competences of the ministries were set out in article 20 of the General Statute on Ministries of the USSR which directed ministries to act in accordance with their work plan (budgetary assignments).<sup>240</sup> The position was confirmed by the decree of the Council of Ministers "On the Procedure for the Creation, Reorganisation and Liquidation of Enterprises, Associations, Organisations and Institutions" which provided that "the creation of enterprises, associations, organisations and institutions shall be made by state agencies within the limits of the financial and material resources assigned to them, the work plans, budgetary assignments and other established limits and norms".<sup>241</sup> Therefore in practice the process of forming state enterprises started with the adoption of the decision to create them, promulgated by the duly empowered state agency on the basis of the requirements of the plan and the

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<sup>235</sup> On the "voluntary" nature of the creation of collective farms, see *supra* Sections 2.4.1 and 4.1.3.

<sup>236</sup> *Supra* n.123 (1988), p.35.

<sup>237</sup> *Supra* n.27 (1950), p.151.

<sup>238</sup> Enterprise Statute, article 6. The Production Association Statute provided for formation by decision of the duly empowered ministry or Council of Ministers. In addition it listed a number of considerations that should have been taken into account when considering whether to create a production association. These stressed the advantages of economies of scale, integration and centralisation of procedures and management (Production Association Statute, article 5).

<sup>239</sup> On the superior organs of state economic organisations see, *Osnovy Upravleniya Narodnym Khozyaistvom* (Yuridicheskaya Literatura:1981), pp.49-52.

<sup>240</sup> Obshchego Polozheniya o Ministerstvakh SSSR (1 *SDZ SSSR* 236). Footnote 1 to article 20 in the *SDZ SSSR* (1 *SDZ SSSR* 241) traces the development of subordinate legislation regulating the formation of enterprises.

<sup>241</sup> Polozhenie o Poryadke Sozdaniya, Reorganizatsii i Likvidatsii Predpriyatii, Ob''edinenii, Organizatsii i Uchrezhdenii, *SP SSSR* (1982), no.25, item 130, article 3.



resources allocated to it from the state budget. This then led to the drawing up of a charter which was then registered and confirmed. Juridical personality arose upon registration.<sup>242</sup>

Soviet civil law adopted the term "termination" to describe the circumstances when a juridical person's existence was discontinued. An enterprise could have been "terminated" by one of two means: "reorganisation" or "liquidation".<sup>243</sup> A reorganisation (through merger, separation or accession) always resulted in a successor organisation, whereas a liquidation did not. The 1961 FPCivL was silent on the question of termination and the civil codes did not provide any specific instances when termination would be required, or for a particular procedure to be adopted. Furthermore, the decree "On the Procedure for the Creation, Reorganisation and Liquidation of Enterprises, Associations, Organisations and Institutions" only contained passing references to liquidation and again did not set out the grounds for liquidation. Reflecting an equivalent provision in the civil codes, article 105 of the Enterprise Statute merely provided that enterprises may be "reorganised or liquidated by decision of the agency which is empowered to form the respective enterprise."

A commentary to the RSFSR civil code noted that "the grounds for liquidation are: the achievement of the purpose for which the juridical person was formed, the expiry of the period for its activities, the inexpediency of its further existence and activity and other reasons".<sup>244</sup> A commentary to the Enterprise Statute explained further that "liquidation of an enterprise takes place in the event that its continued existence is deemed inexpedient."<sup>245</sup> The Soviet civil law textbooks of the period rarely elaborated further, sometimes noting only that a liquidation commission (the body which carried out liquidation) was appointed by the superior state agency or by the director of the organisation (where so duly empowered by the superior state agency).<sup>246</sup>

The absence of any detailed discussion on the procedure for liquidation, or when it was required, suggests that the decision to liquidate an enterprise, like its formation, was, as a practical matter, simply a matter of policy, an exercise of discretion, a mere confirmation,

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<sup>242</sup> Enterprise Statute, articles 6 and 7; Production Association Statute, article 8.

<sup>243</sup> RSFSR CC, article 37.

<sup>244</sup> *Kommentarii k Grazhdanskomu Kodeksu RSFSR* (Yuridicheskaya Literatura:1982), p.65.

<sup>245</sup> *Kommentarii k Polozheniyu o Sotsialisticheskoy Gosudarstvennoy Proizvodstvennoy Predpriyatii* (Izdatel'stvo Yuridicheskaya Literatura:1968), p.297.

<sup>246</sup> See, for example, *Sovetskoye Grazhdanskoye Pravo, Tom I* (Izdatel'stvo Yuridicheskaya Literatura:1979), p.153.



taken without the need for a detailed legal procedure.<sup>247</sup> And as has been argued from within the model of confirmation, the creation and liquidation of the state enterprise was more a question of policy than law. The Soviet state was omnipotent - the representative of the working class interests and the single owner. In accordance with official ideology, its state plan produced the optimal allocation of resources and was drawn up on the basis of objective economics. The profitability of any single unit in the economy was of secondary importance as compared to its role and function within the economy as a whole - indeed the test of "profitability" was not mentioned within the traditional grounds for liquidation.

The market economy concept of liquidation conditions, an inability to pay or service debts, was therefore an irrelevance within the Soviet context. As Ioffe pointed out in his treatise on Soviet civil law that "Although numerous state economic entities cannot exist without governmental subsidies, and numerous collective farms cannot make ends meet when totalling their financial achievements for the economic year, bankruptcy as a purely capitalist phenomenon is alien to socialism and, as a result, it has been left out of Soviet law."<sup>248</sup> It seems that this was not entirely inaccurate. In 1987 Nikolai Ryzhkov, the then prime minister, estimated that approximately 13% of all industrial enterprises were "unprofitable", that is reliant on state subsidies.<sup>249</sup> As such it was rare that enterprises were ever liquidated, and it was "more common"<sup>250</sup> to terminate enterprises by reorganisation which would result in a legal successor and thereby ensure continued use of the existing industrial complex and employment for its employees.

### 3.3 Juridical Personality - The Veil of Legal Autonomy

There was very little discussion in Soviet law textbooks as to why the state enterprise was given the status of a juridical person.<sup>251</sup> Generally, textbooks only described the positive law

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<sup>247</sup> Despite a lack of discussion on the rules for liquidation in most Soviet civil law textbooks, Soviet law did in fact contain rudimentary procedures for the liquidation of enterprises and in particular a list of assets against which claims could be levied (see, for example, RSFSR CCP, articles 408-411). See also *infra* n.270.

<sup>248</sup> *Supra* n.123 (1988), p.37.

<sup>249</sup> *Izvestiya* (30 June 1987), p.4.

<sup>250</sup> *Kommentarii k Grazhdanskomu Kodeksu Kazakhskoi SSR* (Izdatel'stvo Kazakhstan:1988), p.75. One textbook noted "at the present time, juridical persons are usually terminated through reorganisation resulting from new requirements in the area of economic, cultural and state construction" (*supra* n.41 (1986), p.127).

<sup>251</sup> There was no *a priori* reason why state enterprises "had" to be juridical persons - as Teubner noted "nothing prevents the legal system from taking any object whatever - divinities, saints, temples, plots of land, article objects - as points of attribution and giving them legal capacity. Trees particularly are prominent candidates." (Gunther Teubner, "Enterprise Corporatism: New Industrial Policy and the Essence of the Legal Person", *supra* n.223, p.59).



which stated that juridical personality was conferred upon a state enterprise following the confirmation of its charter by the applicable state agency.<sup>252</sup> It has been suggested in this Chapter that juridical personality was used as the framework to develop a legally separate addressee of the plan with the ability to operate on the basis of a separate balance sheet, and in the case of industrial organisations, on the basis of *khozraschet*. It is perhaps for this reason that, as one civil law textbook noted, "juridical personality (a legal subject of civil law) is the necessary and essential element of an enterprise".<sup>253</sup> The ingeniousness of this approach was that although juridical personality meant "separation", providing a separate vehicle for economic activity, it did not entail any specific governance regime *per se* and therefore did not require the state to cede any more control over the micro-economy to this vehicle than it considered appropriate at any particular time.<sup>254</sup>

Juridical personality created pursuant to a state act has traditionally been viewed in terms of the "granting" of a "concession". However in the Soviet context, as has been argued, it is more appropriate to understand the conferring of juridical personality in terms of "confirmation" or "delegation" as opposed to "granting". The state was acting as a "creator" of enterprises, carving-out separated entities from the administrative state and state ownership of the means of production, created for the purpose of carrying out certain defined activities. These juridical persons were very clearly not the result of an independently formed association created by third parties petitioning the state as sovereign for the grant of legal recognition as a collective subject of civil law.

While the *rationale* for juridical personality was undeveloped in Soviet law, the essential *features* of a juridical person were a matter of much debate. Article 11 of the 1961 FPCivL (repeated in the civil codes) set out some of these: "Juridical persons shall be deemed to be organisations which possess solitary property, may acquire property and personal non-property rights and bear obligations in their own name, and be plaintiffs or defendants in court, arbitrazh or arbitration",<sup>255</sup> and later noted as juridical persons: "state enterprises and other state organisations which are on *khozraschet* and having basic and circulating assets

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<sup>252</sup> Supra n.242. "In cases where the need arises to ascertain whether the given collective organisation is a legal person...one must turn to the constituent instrument on the basis of which this organisation was set up. Not infrequently this document contains a direct reference to the fact that the given organisation is a legal person. The rights of a legal person may also be confirmed by the fact that the organisation (its constituent instrument) has been registered by competent bodies" (supra n.182 (1988), pp.15-16).

<sup>253</sup> Supra n.41 (1986), p.137.

<sup>254</sup> "The institute of juridical personality is above all a civil law designation and results in *operative* autonomy of the enterprise in the carrying out of its planned economic activities", [emphasis added] (ibid, p.117).

<sup>255</sup> Repeated *verbatim* in RSFSR CC, article 23.



allocated to them and a separate balance sheet".<sup>256</sup> Article 2 of the Enterprise Statute expanded on the general law providing that: "The socialist state production enterprise, using state property allocated to its operative management or use, shall carry out, with the efforts of its collective under the direction of a superior agency, its production-economic activities (manufacture of products, fulfilment of works, rendering of services) in accordance with the national-economic plan, on the basis of *khozraschet*, shall fulfil obligations and enjoy the rights connected with such activities, shall have a separate balance sheet and shall be a juridical person."<sup>257</sup>

In summary, Soviet textbooks generally noted that juridical status entailed the following four features: (i) organisational unity, (ii) solitary property, (iii) autonomous property responsibility; and (iv) the ability to enter into civil law relations in its own name.<sup>258</sup> While there was much debate as to whether these characteristics were in fact distinct,<sup>259</sup> it is probably more useful to view them as interlocking and interdependent features of an organisation created to give rise to a separate person capable of acting as the addressee of the state plan while at the same time cradled by a governance regime that sufficiently ring-fenced any discretions that arose by virtue of this formal legal autonomy.<sup>260</sup>

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<sup>256</sup> The following were also mentioned in that article as juridical persons in article 11: "institutions and other state organisations which are on the state budget and have a separate estimate and whose directors enjoy the rights of disposing of credits...; state organisations financed at the expense of other sources and having a separate estimate and separate balance sheet; collective farms, inter-collective farms, and other cooperative organisations and their associations...state-collective farms and other state-cooperative organisations.... [and] other organisations in the instances provided for by the legislation of the USSR".

<sup>257</sup> This provision was reproduced almost *verbatim* in article 2 of the Production Association Statute.

<sup>258</sup> For example, supra n.246, p.1136-138; and n.41 (1986), pp.117-119.

<sup>259</sup> The fourth characteristic, the ability to enter into civil law turnover was, until the adoption of the 1961 FPCivL, particularly contentious. Bratus argued that "the deciding precondition and basis [for juridical personality]...was solitary property" (supra n.27 (1950), pp.146) and that there was no need to introduce this fourth characteristic which was in essence a summary of the other three. By contrast, first Genkin (see D.M. Genkin, *Yuridicheskie Litsa v Sovetskom Grazhdanskom Prave*, *Problemy Sotsialisticheskogo Prava* (1939), no.1, pp.91-93) and then Venediktov argued that "autonomous participation in civil law turnover in the capacity as a separate (particular) holder of civil rights and obligations and consequently act in its own name is the decisive criteria" (supra n.57 (1948), p.705).

<sup>260</sup> The interdependence of the various features was particularly evident as the legislation when describing the relevant organisation (see supra n.257) never set out which elements of the description arose as a consequence of its juridical personality and which were simply characteristics of the organisation *per se*. This distinction was particularly opaque in article 2 of the Enterprise Statute quoted above. As a legal matter there was no necessary link between solitary property, *khozraschet* and autonomous responsibility on the one hand, and juridical personality on the other. This was recognised by Venediktov who cited the example of various partnerships in "bourgeois law" which despite having juridical status, also had unlimited responsibility of the partners for its debts (supra n.57 (1948), p.695).



***Solitary Property and Khozraschet*** The basic principle was that "in order to autonomously participate in goods-money relationships and exist as a subject of civil law, an organisation must possess property separated from property of other persons - citizens, organisations and the state".<sup>261</sup> The term "solitary" was used to indicate that although state property was allocated to the enterprise (ie "separated out"), the ownership thereof always remained with the state.<sup>262</sup> The property of a state enterprise was made up of a number of funds or reserves. The charter fund comprised basic and circulating assets of the enterprise. Other funds included the monetary funds (such as a fund for capital investment, and amortisation fund); and incentive funds (such as the production development fund, the fund for social-cultural measures and housing construction).<sup>263</sup>

By conceiving of the industrial organisation in terms of an addressee of the plan, the confirmation model explains the necessity for the "separation" of the property of the state enterprise from that of the state. While juridical personality, strictly construed, was a method for separating out the legal status of the industrial organisation thereby giving it civil law standing, solitary property enabled the juridical person to have the *capacity* for economic autonomy.<sup>264</sup> First, it meant that it could act as a separate economic unit with a separate balance sheet; and secondly, it enabled operation on the basis of *khozraschet*. Enterprises could be allocated separate property and then were required to cover the costs of all future operations from within this property and any revenues generated.<sup>265</sup> Finally, it facilitated the separate evaluation of the economic activity of this organisation; for without solitary property and a separate balance sheet, it would have been impossible to have tested whether its revenue covered its costs.

***Autonomous Property Responsibility*** Autonomous property responsibility was a peculiar feature of the confirmation model that should not be confused with the "market economy" concept of "limited liability". Article 13 (as amended) of 1961 FPCivL provided two principles of responsibility:<sup>266</sup> First, "a juridical person shall be responsible for its own obligations with property belonging to it (allocated to it) on which execution may be levied on the basis of legislation of the USSR and union republics", and secondly, "the state shall not be responsible for the obligations of state organisations having juridical personality and these

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<sup>261</sup> Supra n.41 (1986), p.118.

<sup>262</sup> The concepts of ownership and operative management are considered in more detail infra Section 3.4.2.

<sup>263</sup> The list of funds was more clearly set out in the Production Association Statute at article 39.

<sup>264</sup> The extent of such autonomy would be determined by the governance regime.

<sup>265</sup> On *khozraschet* see supra Section 2.2.

<sup>266</sup> 1961 FPCivL, article 13; and RSFSR CC, articles 32 and 33.



organisations shall not be responsible for the obligations of the state". The civil codes added a third principle: "a state organisation shall not be responsible for the obligations of an enterprise subordinate to it having juridical personality and this enterprise shall not be responsible for the obligations of organisations to which it is subordinate".<sup>267</sup> On the basis of these basic rules the Soviet law principle of autonomous property responsibility seemed in form to be similar to the concept of "limited liability"; however, in substance, they were very different.

Limited liability is essentially a rule relating to insolvency and therefore to risk allocation. As long as a company is paying its debts as they fall due, the status of limited liability is an irrelevance. If however a company is being wound-up, limited liability ensures that creditors of that organisation cannot seek satisfaction for the debts incurred by that organisation from the separate assets of its owners. From a practical and economic point of view there are a number of additional consequences associated with limited liability status in the market economy: the principle of limited liability encourages investment in equity capital (eliminating the risk that other assets of investors could become attached on an insolvency) and it also provides creditors with a "bright line test" as to the financial condition of the juridical person which must be calculated on the basis of its financial condition (as set out in its accounts). Therefore owners of the company do not need to spend time and costs monitoring the assets of other owners as this will not affect the "credit" of the organisation.<sup>268</sup>

Such considerations were largely irrelevant within the context of the Soviet economic system which was based on a single owner of the means of production, determining industrial activity by diktat principally in the form of the state plan. Liquidation was not used as a method for imposing economic discipline through a "market of corporate control" such as in market economies and it was often that Soviet state enterprises unable to pay their debts when they fell due were generally either reorganised or re-labelled an "unprofitable enterprise" and the appropriate subsidies were made from the state budget.<sup>269</sup> Where liquidation did occur, Soviet

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<sup>267</sup> RSFSR CC, article 34.

<sup>268</sup> For a more detailed account of the function of limited liability in market economies see Frank H. Easterbrook and Daniel R. Fischel, *The Economic Structure of Corporate Law* (Harvard University Press:1991), pp.41-44.

<sup>269</sup> The disciplines of *khozraschet* and self-sufficiency were generally subordinated to the needs of the plan if necessary. Indeed in the early days of Soviet industrialisation, all industry was financed from state subsidies as access to foreign capital was restricted and there was no general internal non-state capital market. As Davies noted of the year 1929-1930: "The legislation on *khozraschet* was almost entirely ignored in practice...This reflected the widespread view that with the growth of comprehensive physical planning no real distinction could be made between establishments financed from the state budget and enterprises financed by *khozraschet*" (supra n.12, p.315-316).



law provided that creditors usually only had recourse to cash assets, and not to other property and basic assets that had been allocated to it by way of operative management.<sup>270</sup>

The Soviet concept of autonomous property responsibility was more of an accounting principle than a procedural rule relating to the liquidation of an enterprise and the division of assets. As it has been argued, the rationale behind solitary property and autonomous property responsibility as elements of juridical status was to create an organisation that could act as an appropriate addressee of planned instructions, capable of operating and being evaluated on its own terms through the concept of a separate balance sheet and *khozraschet*. *Khozraschet* would simply not have been able to operate effectively unless, as an accounting matter, the industrial organisation was treated as a separate organisation. Autonomous property responsibility was aimed at facilitating the day-to-day evaluation of its economic performance and role by the state planners.

And so while the "principles" of autonomous property responsibility and limited liability seem to set out a similar attribute, the model of confirmation and its explanation of the role of the confirmation enterprise illustrates that in functional terms both these rules were used by different types of economy to address different concerns.

### 3.4 Governance - Economic Dependence

Four distinct roles of the state have been identified in this Chapter. Each of them distinguish a different element of a governance regime by which the Soviet state ensured the capacity to exercise near total control over its "autonomous" juridical persons. Furthermore, by focusing on each role and its evolution during the period to 1990, the analysis of the nature of the "new" industrial organisations introduced during this period, and the retreat of the state from direct management of the industrial economy, becomes deeper and sharper.

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<sup>270</sup> See RSFSR CC, article 101. Primary recourse of "creditors" for unsatisfied debts was to the monetary assets in credit institutions and only then could creditors seek recourse against the property in operative management of the enterprise (RSFSR CCP, articles 408-411). Nevertheless there were certain assets of the enterprise upon which execution could never be levied. Article 22 of 1961 FPCivL provided that "enterprises, buildings, installations, equipment, and other property relegated to the basic assets of state organisations may not be the subject of pledge and execution may not be levied thereon in respect of the claims of creditors." (This provision was reproduced *verbatim* in the civil codes: RSFSR CC, article 98). This part of article 22 of the 1961 FPCivL was amended by deleting the word "enterprises" from the list by an edict of the Presidium of the Supreme Soviet of USSR (*Vedomosti SSSR* (1981), no.44, item 1184). The amendment was then made to the corresponding provisions of the civil codes. The codes of civil procedure, while reflecting the substance of article 22, went further, prohibiting any claims against the seed and fodder reserves, as well as other reserves and assets necessary for the carrying out of their normal activities. Levying execution on property of state enterprises (except monetary assets) located within the state budget was also prohibited.



*State as Creator-Owner* The state as creator or founder of the enterprise had available to it the "traditional" governance structures for maintaining control. As founder, the state could draw-up the charter and could specify therein the purposes of its activities and ensure that the scope of the management's discretion was suitably ringfenced.

*State as Property-Owner* In addition to being the founder of the enterprise, the state retained ownership of all of the property allocated to the enterprise. Therefore in addition to possessing the right to impose limits on management's powers in the charter, the state could also impose limits on the way that the management used the property "of" the enterprise - for although it was "separated" from the state, it remained in the ownership of the state.

*State as Legal Sovereign* The state was also the legal sovereign and therefore could enact legislation to determine the framework of the industrial organisations generally, as well as to require specific conduct by legal diktat.

*State as Economic Sovereign* In addition to being the source of all law, the Soviet state (as quasi feudal overlord) was also the single unitary owner of all of the means of production. As owner not just of the property of the enterprise but also of the entire economy, it could promulgate general plans and issue specific administrative instructions that bound every enterprise with each other in a single economic network of economic contracts.

#### 3.4.1 *The Charter and Special Legal Capacity*

The Enterprise Statute required each enterprise to have a charter confirmed by the state agency which took the decision on its formation.<sup>271</sup> The charter was to contain: the name (or number) of the enterprise and its location (postal address); the name of the state agency to which the enterprise was directly subordinate (the superior state agency); the subject and purpose of the activities of the enterprise; details of its charter fund; a provision that the enterprise operated on the basis of the Enterprise Statute and that it was a juridical person; and the name of the official heading up the enterprise (the director, manager, boss).<sup>272</sup> The charter was also permitted to contain additional provisions "not contrary to legislation". These usually specified any peculiarities relating to the activities of the enterprise.

As an alternative to a charter, but only in the specific instances provided for by legislation, enterprises could be governed by "general statute".<sup>273</sup> A general statute was used as the basic

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<sup>271</sup> Enterprise Statute, article 7; Production Association Statute, article 8.

<sup>272</sup> Ibid.

<sup>273</sup> Enterprise Statute, article 7. There was no equivalent for the production association (see Production Association Statute, article 8). Sometimes they were referred to as "Model Charters".



constitutional document for *all* state enterprises operating within a particular sector of the economy.<sup>274</sup> Braginsky noted that "...the difference between a charter and a statute is purely terminological and in content, both acts fully coincide."<sup>275</sup> There was however one important difference in their process of adoption: a general statute had to be adopted by decree of the Council of Ministers (ie the government) of the USSR. While the Soviet "general statute" seemed similar in form to "model articles of association" in market economies,<sup>276</sup> the function of these general statutes was very different. Soviet general statutes should be understood in terms of restriction rather than prescription. Market economy model charters generally provide default rules that apply where owners do not "contract out" of them. By contrast, rather than aiming at the devolution of discretions to the lowest level, the Soviet general statutes simply abstracted and elevated the responsibility for drafting the constitutive documents of state enterprises in a particular sector from the local duly empowered state agency to the government of the USSR itself. Inferior state agencies had no right to contract out of terms of the general statutes when creating state enterprises subordinate to them and established in a sector governed by a statute, other than where residual discretion was expressly provided for by legislation.

After having taken the decision to create a state enterprise in accordance with the requirements of the relevant plan, the charter was adopted, confirmed and registered as a precondition to juridical status.<sup>277</sup> The drawing-up of the contents of the charter provided the first opportunity of the state to ensure that discretions delegated to the manager of the state enterprise were carefully crafted and restricted as appropriate. Control was then achieved by the operation of the Soviet law of *vires*.

The first aspect of the *ultra vires* rule applied generally. Under Soviet law, all "rights" of any civil law subject, including of a state enterprise, were conditional, restricted by reference to the way that they were exercised. As article 5 of the 1961 FPCivL provided that "civil rights shall be protected by law, except in the instances when they are exercised contrary to the purpose of those rights in a socialist society in the period of the construction of communism". Furthermore, transactions "performed with a purpose contrary to the interests of a socialist

<sup>274</sup> Supra n.244, p.52.

<sup>275</sup> Supra n.182 (1988), p.17.

<sup>276</sup> See, for example, "Table A" in English company law (Companies Act 1985, Table A (SI 1985/805, Schedule)).

<sup>277</sup> Supra n.242.



state and society" were simply void.<sup>278</sup> These provisions were an expression of the wider Soviet law principle that everything was prohibited unless it was expressly permitted.

The second aspect of the *ultra vires* rule was more specific and was developed through the concept of "special legal capacity". Each charter had to include a purpose clause specifying the purpose and subject of activity of the particular juridical person. Article 12 of the 1961 FPCivL provided that "a juridical person shall possess civil legal capacity in accordance with the purposes established for its activities."<sup>279</sup> Transactions "performed contrary to these specific purposes" were void.<sup>280</sup>

A reading of the Soviet law commentaries on special legal capacity reaffirmed the argument that this is best understood as a part of the governance regime of state juridical persons rather than simply as an abstract principle of civil law. Venediktov explicitly noted that "the principle of special legal capacity of juridical persons was in the USSR (in contrast with bourgeois countries) a direct consequence and reflection of socialist planning".<sup>281</sup> Another textbook explained that "juridical persons are created for definite purposes and the state controls how and in what amount they are carried out...".<sup>282</sup> Limitations on capacity ensured that "the possibility of deviation from the tasks set for it is removed."<sup>283</sup> The 1965 commentary to the Kazakhstan Civil Code noted simply that "the nature of a planned economy necessitates a precise delineation of the sphere of legal actions which must and may be performed by socialist organisations, using all their resources on the initiative of the entire collective for the effectuation of their purposes."<sup>284</sup> However, although such commentaries hint at its importance, it is only when the state enterprise is presented within the confirmation model that the notion of special legal capacity can clearly be viewed as a key element in a governance regime that extends beyond the idea of mere *vires*, to an explanation based on the function of juridical personality itself as the addressee of the plan balancing autonomous and controlling influences.

Soviet law distinguished conceptually between rights based on "material criteria" (the derivation of rights from the subject and purpose of its activities) and those based on "formal

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<sup>278</sup> RSFSR CC, article 49.

<sup>279</sup> This provision was reproduced in the various civil codes without substantial amendment: RSFSR CC, article 26.

<sup>280</sup> RSFSR CC, article 50.

<sup>281</sup> Supra n.57 (1948), p.686.

<sup>282</sup> Supra n.41 (1986), p.120.

<sup>283</sup> Ibid., p.120.

<sup>284</sup> *Kommentarii k Grazhdanskomu Kodeksu Kazakhskoi SSR* (Izdatel'stvo Kazakhstan:1965), p.57.



criteria" (a list of fixed rights independent of purpose).<sup>285</sup> As we have seen, civil law rights under Soviet law were based on a material criteria and were therefore always derivative, constrained by the purpose for which they were intended to be exercised. It is perhaps for this reason that Soviet legislation on enterprises only required the "subject of activity" to be included in the charter and not a list of rights.

A purposive theory of the existence of rights, coupled with the operation of the *ultra vires* rule, meant that the Soviet regime had the flexibility both to curtail and to broaden permitted discretions of a juridical person merely by changing the official "interpretation" of the purpose clause. A strict approach could be taken as was illustrated by decisions of the Soviet courts in invalidating transactions as contrary to the purposes specified in the charter.<sup>286</sup> Alternatively an expansive approach could be taken, illustrated by the doctrine of "associated" ("*soputstvuyushchyi*") purposes and rights: activities "associated" with the purposes specified in the charter would therefore be valid and permitted.<sup>287</sup> Such "associated actions" were typically activities aimed at providing workers with certain benefits such as schooling, housing and the like. Article 2 of the Enterprise Statute and Production Association Statute was explicit on this point and provided that an enterprise or association shall "enjoy the rights connected with such activities".

Any "formal" list of rights contained in the legislation and in the charters of the time should be understood in this context. As a commentary to the RSFSR civil code noted "it is not possible to provide in the charter an exhaustive list of transactions that may be performed in accordance with the purposes of the juridical person and deemed to be valid: a detailed list is in any event incomplete...a juridical person may act in any legal relations corresponding to the purposes specified in the charter".<sup>288</sup> Therefore it was not any list of rights in the charter that would be determinative, instead, the enterprise simply possessed all those rights associated with its purpose of activities and had to exercise such rights consistently therewith. Nevertheless, it is important to note that both the Enterprise Statute and the Production Association Statute devoted an entire section (Section IV) to the rights of the enterprise (or

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<sup>285</sup> Supra n.182 (1988), p.18.

<sup>286</sup> See, for example, the use of the *ultra vires* decision to invalidate a contract made between a collective farm and a citizen as being contrary to the provisions of its charter. (*Sbornik Postanovlenii Plenuma Verkhovnogo Suda SSSR 1924-1963* (Izdatel'stvo Izvestiya Sovetov Narodnykh Deputatov SSSR:1964), p.78).

<sup>287</sup> Supra n.27 (1958), p.211.

<sup>288</sup> Supra n.94, p.53.



association).<sup>289</sup> These included, in the Enterprise Statute, rights in the domain of planning; in the domain of capital construction and capital repair; in the domain of improving technology and production technology; in the domain of material-technical supply and sale; in the domain of finances; and in the domain of labour and wages. As a matter of practice, the charter often also contained a list of rights. It is curious within the context of Soviet law and the rejection of "formal criteria" as the basis for rights that such lists in both the legislation and the charter should have been set forth in such detail. The listing of rights in this way was probably used to indicate an attempt to decentralise discretions, but more often that not, the rights were not just permissive, but were expressed as requirements to act in a particular way, and therefore were a function of the third feature of the governance regime, coercive law.<sup>290</sup>

Despite the fact that both Soviet legislation and the charters were essentially state acts, the listing of rights was in no way an attempt to create exceptions to the general concept that rights were derivative. There were no discussions in the Soviet legal literature of the time that suggested that these lists constituted official recognition of special regimes of operation and the existence of inalienable rights.<sup>291</sup> In the opinion of Ioffe and Maggs, "despite the great number of such norms, they do not give the impression of real autonomy of production associations. Numerous economic actions demand direct permission or coming to agreement".<sup>292</sup>

While the charter, through the *ultra vires* rule, was the legal straightjacket for the exercise of discretions by management, it also set out the other elements of the governance regime: the nature of the property allocated to the enterprise and the management structure.

### 3.4.2 *Operative Management - Property Without Ownership*

One of the unique aspects of the governance regime of the confirmation model was the concept of the continuing ownership "of" the property of the confirmation enterprise by its founder, the state. This allowed for control over its activities through the direct ownership of

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<sup>289</sup> This represented a significant part of each of those statutes as the Enterprise Statute was divided up into only six sections and the Production Association Statute into five. The listing of rights in legislation dates to the decree "On the Broadening of Rights of Directors of Enterprises" adopted in 1955 which similarly set out the parameters of the discretions of the director (O Rasshirenii Prav Direktorov Predpriyatii (9 August 1955) in *Resheniya Partii i Pravitel'stva po Khozyaistvennym Voprosam, Tom 4* (Izdatel'svto Politicheskoi Literatury:1968), p.244).

<sup>290</sup> See *infra* Section 3.4.3.

<sup>291</sup> The question of whether a charter approved and registered by the Soviet state could contain exceptions from prevailing legislation that had the status of law is discussed further in the context of joint enterprises, *infra* Section 5.3.3.

<sup>292</sup> *Supra* n.172, p.151 *et seq.*



its property and the ability therefore to place an additional layer of restrictions upon the management's use of it.

The "orthodox" explanation for continued state ownership of the property allocated to industrial organisations was developed in Soviet legal literature in terms of the Marxist ideological necessity to preserve state ownership of the means of production.

It has however been argued that operative management had two additional functions. First, operative management was an integral part of the solution to the question of the management of the micro-economy posed in the context of a macro-economy based on the plan. Operative management, while preserving state ownership, enabled the "separating out" of property to juridical persons. This in turn facilitated operation as discrete actors and addressees of the plan based on separate balance sheets and *khozraschet*. Secondly, operative management provided an additional element in the governance regime of the confirmation enterprise.

The term "operative management" appeared in the 1961 FPCivL by virtue of an amendment in 1981 to article 26,<sup>293</sup> although the theoretical framework had been developed much earlier, with the classic elaboration by Venediktov in his work on state socialist ownership.<sup>294</sup> Indeed subordinate legislation had for some time contained references to the term (including the Enterprise Statute and the Production Association Statute).<sup>295</sup>

Having proposed in this Chapter the four different roles of the Soviet state and how each role was identified with a particular element of the governance regime of the confirmation enterprise, it is immediately (and curiously) apparent that the drafting of the amended article 26 of the 1961 FPCivL implicitly incorporated each of these: it provided that "property, allocated to state...organisations, shall be in the operative management of these organisations who shall carrying out the right of possession, use and disposition of the property [1] within the limits established by law, [2] in accordance with the purposes of its activities, [3] planning tasks and [4] the designation of the property."<sup>296</sup> The limits established by law reflected the state's role as legal sovereign, the purposes of activities reflected the state's role as creator-

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<sup>293</sup> O Vnesenii Izmenenii i Dopolnenii v Osnovy Grazhdanskogo Zakonodatel'stva Soyuza SSR i Soyuznykh Respublik, *Vedomosti SSSR* (1981), no.44, item 1184. Corresponding amendments were later made to the civil code provisions.

<sup>294</sup> *Supra* n.57 (1948), p.323 *et seq.*

<sup>295</sup> On operative management generally, see V.S. Yakushev, *Pravo Operativnogo Upravleniya kak Institut Khozyaistvennogo Zakonodatel'stva*, *SGiP* (1978), no.4, p.78; S.N. Bratus, *O Sootnoshenii Sotsialisticheskoi Sobstvennosti i Prava Operativnogo Upravleniya*, *SGiP* (1986), no.3, p.19.

<sup>296</sup> This provision was included almost *verbatim* in article 8 of the Enterprise Statute and article 14 of the Production Association Statute.



owner; the planning tasks reflected the state's role as economic sovereign and the designation of property reflected the state's role as property-owner. More broadly, operative management was a product of the basic principle of the Soviet state that everything was prohibited unless permitted, and as such, state property allocated to the state enterprise could therefore not be used for any purpose, other than as prescribed by law, its purposes, planning and designation.

These restrictions on "the operative manager" can be contrasted with the restrictions imposed on an "owner" by article 19 of the 1961 FPCivL which stated only that "the right of possession, use and disposition of property within the limits established by law shall belong to the owner". Therefore as Ioffe explained "the owner can be limited in his triad of rights only by the law, while other holders of the right to possess, use and dispose can be restricted not only by the law but also by the owner himself".<sup>297</sup> This explanation, while accurate, should be expanded in its understanding by taking into account the multi-faceted features of the "owner himself" (ie the different roles of the state) and the fact that each of those features was actually expressed in the amended drafting of article 26.

The argument that operative management must also be understood as an element of the governance regime is strengthened by an understanding of the procedure for the "allocation" of property into the operative management, and the law relating to the obligations of the operative manager. Allocation of property into operative management was effected not by the civil law of contract but by an "administrative act".<sup>298</sup> As a consequence, the legal characterisation of the relationship between the state (owner of property) and the enterprise (operative manager) was not a civil law relationship between equals (such as between parties to a contract of lease) but an administrative relationship between superior and inferior parties. It followed that an enterprise to which property was allocated by way of operative management "shall not only have the right but also the *obligation* to use the property allocated to it in accordance with the purposes of its activities, planning tasks and the designation of the property. Failure to comply with the designation of the property will be a violation of state discipline and shall result in responsibility."<sup>299</sup>

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<sup>297</sup> Supra n.123 (1988), p.93.

<sup>298</sup> The procedure for the disposition of state property to organisations as basic or circulating assets was set out in article 22 of 1961 FPCivL and then developed in the civil codes (RSFSR CC, articles 96 and 97) as well as subordinate legislation (eg O Poryadke Peredachi Predpriyatii, Ob''edinenii, Organizatsii, Uchrezhdenii, Zdanii i Sooruzhenii, *SP SSSR* (1979), no.26, item 172 and *SP SSSR* (1980), no.11, item 85 (with the same name)). See as to the detail of the procedure, supra n.41 (1986), pp.347-350.

<sup>299</sup> Supra n.250, p.135. [emphasis added].



Therefore, while indeed operative management was used within the Soviet law on ownership to preserve the ideological requirement of state ownership of the means of production, at the same time it functioned to enable state-owned juridical persons to operate within the national economy with separate balance sheets, and perhaps more importantly, was a key component in the governance regime of those enterprises embodying all four roles of the state within it.

### 3.4.3 *Unitary Ownership, One-Man Management and Coercive Law*

Juridical persons have to exercise their civil law capacity through representative bodies of natural persons - collective or individual. Companies in a market economy are the focal point for numerous different interests including those of its shareholders, directors, creditors and employees, and therefore the structure of these representative bodies and the theories explaining the nature of their various discretions and competences are often complex. By contrast, the Soviet state enterprise had a much simplified structure which reflected the logic of the confirmation model and the unitary state.

There was no concept of shareholder or equity participation by a fragmented group of interests including directors and workers. The state was the single owner of the means of production and the state represented the interests of all-people. Article 2 of the 1927 Trusts Dekret stated that "a state industrial trust shall be deemed to be a state industrial enterprise organised on the basis of a special charter in the form of a separate economic unit with the rights of a juridical person and *a capital structure not divided into shares*" [emphasis added]. Consequentially Venediktov noted that "workers and employees of a state juridical person do not directly participate in the formation of its property through contributions, shares etc and have no rights to its property; they [only] receive wages as compensation for their work and not in the form of a proportionate share in the revenues of the juridical person; and if they participate in the management of the business of the juridical person then it is in the capacity of an official fulfilling the administrative and labour duties allocated to them by the state, and not as a member of the juridical person."<sup>300</sup>

The concept of the unitary owner was reflected in the principle of one-man management, thereby allocating primary responsibility for the operations of the enterprise in a single person who was an administrative appointee. This structure facilitated the alignment on an on-going basis between the actions of management and the requirements of the state.

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<sup>300</sup> Supra n.57 (1948), p.688. This (perhaps) can be contrasted with the internal organisation of the collective farm (see supra Section 2.4.2).



The 1961 FPCivL did not mention the management structure of juridical persons, and the civil codes only briefly provided that "juridical persons shall acquire civil rights and bear civil obligations through its organs acting within the limits of the rights granted to them by law or charter (or statute)" and that "the procedure for the appointment...of the organs of juridical persons shall be determined by the charter (or statute)".<sup>301</sup> The state acting as legal sovereign through the provisions of the Enterprise Statute set out the structure in more detail. Article 89 provided that "the director (or head, manager) shall head an enterprise" and that "the director of an enterprise shall be appointed to or removed from the post by the superior agency". Article 90 then set out the principle of one-man responsibility: "the director shall organise *all* the work of the enterprise and bear *full* responsibility for its condition and activities" [emphasis added]; and further that "the director shall act in the name of the enterprise without a power of attorney represent it in all institutions and organisations, dispose of the property and assets of the enterprise in accordance with the law, conclude contracts and issue powers of attorney (including the right of delegation), open checking accounts and other accounts of the enterprise at banks." The Enterprise Statute also contemplated the appointment of "deputy directors and other leading workers", however it was clear that the "administration of the enterprise" was "in the person of the director".<sup>302</sup>

The Production Association Statute provided a similar structure although this statute did appear to contain more references to the concept of collegiality and rights of the labour collective through the introduction of a "council" as a decision-making body. Article 17 provided for the concept of a one-man manager,<sup>303</sup> and article 18 provided for equivalent rules on one-man management and one-man responsibility to those of article 90 of the Enterprise Statute. However, this was tempered by the provision that stated "a production association...shall be managed on the basis of the proper combination of one-man management and collegiality in the discussion and decision of all questions relating to directing the activity of the association".<sup>304</sup> Despite these references to a "council" and the principle of collegiality along the lines of the collective farm type structure, the principle of one-man management was still directly referred to in the Production Association Statute. The council was in fact chaired by the general director, its decisions were generally implemented by the general director, and in the event of a disagreement between the general director and

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<sup>301</sup> RSFSR CC, article 28.

<sup>302</sup> Enterprise Statute, articles 92 and 95.

<sup>303</sup> "A director general (or director) acting on the basis of one-man management shall head the association...[and] shall be appointed to and removed from the post in the procedure determined respectively by the ministry (or department) of the USSR or the union republic council of ministers".

<sup>304</sup> Production Association Statute, article 16.



the council, the view of the general director prevailed.<sup>305</sup> It is for this reason that Ioffe and Maggs concluded that "from all possible viewpoints, production associations are managed by one-man leadership and not by combination of one-man leadership with collegiality as it is provided by Art. 16 of the Statute on the Production Association".<sup>306</sup>

The concept of unitary ownership and one-man management made the issue and structure of management relatively straightforward. There was no need for a complex structure of balancing different interests. The state nominated its single appointee, as political dictatorship was replicated at the level of the enterprise. Western corporate law governance questions such as monitoring, the separation of ownership from control, collective action and the like were collapsed within a structure that was defined by its relative simplicity and crude strength: one owner appoints one manager. And it was of course unitary ownership that enabled Soviet law to dispense with the concept of the ownership interest and with it a critical legal device that would have necessitated a precise elaboration of the nature of the legal relationship between the owner (*qua* owner) and the juridical person.

As has been stressed throughout this Chapter, the state as unitary owner acted in various capacities. It was, at the same time, the owner of the enterprise, its property, and legal and economic sovereign. Perhaps the most powerful lever open to the Soviet state was its capacity to act in its dual sovereign role. The use of legislation and planning instructions meant that the sovereign state could adopt enactments either on state enterprises generally, through adoption of generally applicable statutes and the state plan, or specifically by edicts and decrees addressed only to an individual enterprise. Such enactments coerced management with the full force of law or administrative order to act in a specific manner and further, could be used to provide the legal legitimation for the replacement of management.

In a market economy, the economic stimuli (including the market for corporate control) incentivise certain types of economic behaviour such as profit maximisation, increase in efficiency, investment in technology and the like. As has been described, the Soviet economy constantly struggled to engender *systemic* incentivisation of this type of economic behaviour. While the market economy provides structural incentives for certain "economic" behaviour, the Soviet state found this very difficult to reproduce within the system of a command economy. As such, the Soviet state sought to coerce this type of "economic" behaviour by diktat through the crude governance regime which included simple legal and administrative commands to act "economically".

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<sup>305</sup> Production Association Statute, articles 26 and 27.

<sup>306</sup> Supra n.172, p.151.



The Enterprise Statute contained a whole section (Section III) devoted to "Production and Economic Activity of the Enterprise". This section simply listed the types of behaviour that the state enterprises were "obliged" to pursue as a matter of legal obligation. For example, the Enterprise Statute provided that "the enterprise shall ensure high quality, reliability, and durability of products". Such a legislative requirement was considered necessary (in addition to the other elements of the governance regime open to the state) presumably because this type of behaviour ran contrary to the structural incentives of the command economy where orders were guaranteed, the liquidation of enterprises was exceptional, and workers' jobs were secure. It is probably in light of such adverse economic stimuli that Section III was inserted which also included obligations on the enterprise to make capital repairs to equipment, carry out research and development, build up reserves of raw materials, produce and deliver goods in a timely manner, "dispose of its own financial resources, ensuring the maximum economies in the expenditure of assets", improve its management structure and labour conditions, train workers and provide them with housing.<sup>307</sup>

It has been argued that the governance structure of the state enterprises is best understood by distinguishing the four roles of the Soviet state (as creator-owner, as property-owner, as legal sovereign and as economic sovereign) and broadly conceptualising the state enterprise within the context of the model of confirmation. Traditional governance structures based initially upon the adoption of a charter, and then upon continued monitoring by way of the voting system, were obviated in the context of an enterprise where monitoring was carried out through particular Soviet methods of control. Although constituted as a separate juridical person for reasons already discussed, the Soviet state retained direct control of this organisation through confirmation - confirmation of the contents of the charter, including the description of its subject and purpose of activity; the confirmation of the designation of its property thereby imposing direct limits on the use of its property held by way of operative management; confirmation of the appointment and dismissal of its one-man manager; and finally, the confirmation of legislation and administrative orders which as a matter of law and diktat imposed obligatory requirements upon the management of these enterprise.

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<sup>307</sup> This section did not appear in the Production Association Statute, although there can be little doubt that these economic and social obligations were still relevant. The Production Association Statute did have an article relating to "the principle tasks of a production association" (article 3) where many of the same types of issues were mentioned.



### 3.5 Conclusion

The question of the nature of the Soviet state enterprises and associations can be tackled from various perspectives. This Chapter has sought to develop a model through which the essential elements of their function and operation can best be analysed and explained. The aim has been to provide an heuristic tool that highlights the unique and central characteristics of the state enterprise and production association, a number of which have broadly been overlooked by commentators to date.

It is hoped that the reconceptualisation of the Soviet state enterprise and production association within the confirmation model will lead to a better understanding of their nature as well as provide a starting point for their comparison with, not only functionally equivalent industrial associations in market economies, but also with the new industrial organisations that were to emerge in the Soviet economy during its final years.



#### 4. THE BRIDGE - CONTRACT-BASED ASSOCIATIONS WITHOUT JURIDICAL PERSONALITY

*"Like a bridge over troubled waters..."*

Paul Simon

The role of the contract for joint activity has largely been overlooked in the "history" of Soviet industrial organisations. After all, in 1985, Soviet law classified this form of association simply as a special type of contract without giving rise to a juridical person.<sup>308</sup> It was not mentioned in the 1961 FPCivL, and its regulation was only set out in a short chapter in the civil codes on "Joint Activity". It was presumably considered to be too specific to merit a reference in the 1961 FPCivL, indicating that in conceptual terms, the contract for joint activity was more a question of detail in the Soviet law of obligations, rather than a basis for the elaboration of principle.

However, by analysing the development of the industrial organisation in terms of the models proposed in this study, it will become apparent that the "new" industrial organisations which emerged in the Soviet economy during the *perestroika* era owed an enormous debt to the contract for joint activity. This somewhat ignored form of association provided the conceptual thread between what has been called the confirmation model, the contract-based concession model, and the participation model. And, in theoretical and historical terms, the contract for joint activity linked not only these three models, but also provided the only bridge between pre-revolutionary Russian associations and Soviet industrial organisations; as well as between Soviet agricultural organisations and Soviet industrial organisations. For despite the change in terminology, a "new" history of the contract for joint activity can be written, tracing its roots back to the artel partnership of pre-revolutionary Russian law which both fathered the collective farm organisations as well as the simple partnership of the Soviet 1922 RSFSR Civil Code.

##### 4.1 Background - 1922 RSFSR Civil Code, Chapter X: The Simple Partnership

Pre-revolutionary Russian law distinguished a number of different types of trade partnership including the artel partnership, the full partnership, the partnership on belief, and the joint-stock partnership.<sup>309</sup> The artel partnership was defined in Section 2198 of Volume X, Part 1 of

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<sup>308</sup> Therefore, in this Chapter 4, the contract for joint activity is referred to as an "association" rather than an "organisation" (the latter being the generic term used in Soviet law for the juridical person).

<sup>309</sup> Supra n.20, p.110.



the 1914 edition of the Digest of Laws as "a partnership organised for the performance of definite works or the pursuit of definite trades, as well as for the rendition of services and the performance of duties by the personal labour of the partners on their common account, all of them being responsible jointly and severally".<sup>310</sup> It was an association whose rationale was based upon personal participation, combining the complementary skills of the partners themselves, rather than an association of capital for investment purposes. Although Shershenevich was of the view that pre-revolutionary trade partnerships generally gave rise to juridical persons, he did note that there was some debate as to the particular juridical status of the artel partnership and the full partnership.<sup>311</sup>

Drawing upon this body of pre-revolutionary law, Chapter X of the Soviet 1922 RSFSR Civil Code on "Partnerships" included provisions relating to the simple partnership (the new name for the artel partnership) as well as the full partnership, the partnership on belief, the partnership with limited responsibility and the joint-stock society (share partnership).

The simple partnership was defined in article 276 of the 1922 RSFSR Civil Code as a contract,<sup>312</sup> whereby two or more persons joined their contributions together for the achievement of a common economic goal.<sup>313</sup> Again this contractual association stressed the element of personal participation. The 1922 RSFSR Civil Code was silent on the question as to whether this contract gave rise to a juridical person.

The provisions of the 1922 RSFSR Civil Code on the simple partnership<sup>314</sup> broadly adopted the terminology of contract and common ownership rather than juridical personality.<sup>315</sup> They referred to "contributions" ("*vkladi*") of partners which became the "common ownership of the partners" ("*obshchei sobstvennost'yu tovarishchei*") in which each partner had a

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<sup>310</sup> Quoted supra n.22 (1948), p.701, n.42 therein).

<sup>311</sup> Supra n.309, pp.107-9. The concept of the "artel form" in pre-revolutionary Russian law not only found expression in the artel partnership of the industrial economy as regulated by Section 2198, but also in a specific type of cooperative agriculture which was later to become the basis for the structuring of Soviet collective farms. This Chapter focuses on the development of the pre-revolutionary artel in the industrial economy through the simple partnership and eventually to the contract of joint activity. The significance of the artel in the agricultural sector is outlined briefly supra Section 2.4.1 and infra Section 6.1.3.

<sup>312</sup> Article 284 of the 1922 RSFSR Civil Code explicitly referred to the "partnership contract"; and indeed, Chapter X was contained within Section 3 of the 1922 RSFSR Civil Code on "The Law of Obligations" thereby hinting at the contractual basis for all partnerships created thereunder.

<sup>313</sup> On the question of what was sufficient to constitute a "common economic goal", see supra n.182 (1928), pp.773-774.

<sup>314</sup> 1922 RSFSR Civil Code, articles 276, 278-281, 286 and 287.

<sup>315</sup> See supra Section 2.6. The 1922 RSFSR Civil Code also contained provisions generally on common ownership (article 61 *et seq*).



participatory share ("*dolei*"). However, the provisions also, in places, referred to a reified concept of the partnership thereby suggesting that perhaps it did after all have juridical personality (for example through the use of phrases such as "the contributed property of the partnership" ("*skladochnogo imushchestva tovarishchestva*") (which, in the absence of juridical personality, "should" have been a reference to contributed property *of the partners*)). Voting was carried out on the basis of unanimity unless the partnership contract specifically contemplated majority voting, in which case it was required to take place on the basis of one partner-one vote "and not according to the amount of contributions".<sup>316</sup> Partners bore responsibility for obligations in proportion to their "participatory share participation in the partnership" ("*s dolei uchastiya v tovarishchestve*"). Again this reference to participating share participation *in* the partnership suggested a reified association (i.e. the existence of a juridical person). In addition to the provisions relating to the status and property regime of the simple partnership, the 1922 RSFSR Civil Code also included rules relating to the sharing of profits and losses, and for liquidation.<sup>317</sup>

The silence in the civil code on the fundamental question of juridical personality precluded a clear analysis of the legal structure of the simple partnership. While the terminology suggested a common ownership structure based on contract without giving rise to a juridical person, the legislation did not expressly state this. The analysis was also confused by references to the reified partnership as if it had, or could have had, independent juridical status coupled with the use of inconsistent terminology that might have been construed as terms to be used for the ownership interest of this reified simple partnership (such as "participatory share" or "participatory share participation").

Ultimately, the silence as to the juridical status of the simple partnership in the 1922 RSFSR Civil Code (and the fact that the 1922 RSFSR Civil Code explicitly stipulated that the other types of partnership did give rise to juridical persons) was interpreted to mean that the formation of a simple partnership did not result in the creation of a juridical person. In fact

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<sup>316</sup> The structure of one partner-one vote irrespective of size of any contribution was also evident in the internal structure of the artel-based collective farm where collective farmers had one vote at the general meeting irrespective of the size of their membership fee paid or the amount of their property socialised upon entry into the farm (see *supra* Sections 2.4.1 and 2.4.2).

<sup>317</sup> Termination was specified to occur as a result of various circumstances including the death of a partner, the expiration of the specified term of the contract, the achievement of the purposes for which the contract was entered into and, in certain circumstances, upon the demand of creditors (1922 RSFSR Civil Code, article 289).



the Plenum of the Supreme Court in its decision of 21 July 1924 even held that juridical persons could not participate as partners in a simple partnership.<sup>318</sup>

The legislation on the simple partnership was an early example of the failure of Soviet law to sufficiently characterise the ownership relationship between participants in an association and the association itself. This failure more generally can be seen in part as a consequence of the failure to develop an understanding of the concept of the ownership interest of an association where ownership is fragmented and a juridical person is formed. While unimportant in the context of the command economy where the logic of the overlapping governance regimes of the confirmation model prevailed, this myopia in relation to the concept of the ownership interest would endure through into the contract for joint activity and thereafter into the economy of the *perestroika* years with profound significance for the history of the foundations of the industrial organisations of the 1990s.

Chapter X was amended extensively in the late 1920s, broadly as a result of the increasing importance of "new" state-owned socialist industrial organisations: the trust, the syndicate, the association and the state enterprise.<sup>319</sup> Almost all references to joint-stock partnerships were removed by 1931 and the provisions relating to the other types of partnership (the simple partnership, the full partnership, the partnership on belief and the partnership with limited responsibility) were also amended but not in such a radical fashion.<sup>320</sup>

Although Chapter X was never amended again, in practice, from the 1930s onwards, these partnerships were rarely created. As one commentator put it "in 1929 in connection with the liquidation of the capitalist elements in the USSR, all private partnership associations, created for entrepreneurial activity, terminated their activity. In 1930, joint-stock societies, both state and mixed, were re-organised into enterprises with capital undivided into shares. In this manner, all forms of partnership contracts, created for entrepreneurial activity, lost their significance in Soviet law."<sup>321</sup> However, although this suggests that all partnership contracts

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<sup>318</sup> Supra n.22 (1928), p.775.

<sup>319</sup> These are examined supra Chapter 3.

<sup>320</sup> In 1928 section 5 of Chapter X of the 1922 RSFSR Civil Code on the "Joint-Stock Society (Share Partnership)" was almost deleted in its entirety (Ob Izmenenii Statei 322, 323, 324, 325 i 326, Otmene Statei 323-a, 323-b, 323-v, 323-g, 327-366 Grazhdanskogo Kodeksa RSFSR i ob Utverzhdenii Prilozhenii k Statei 322 i 326 Grazhdanskogo Kodeksa RSFSR, *SU* (1928), no.38, item 282, and Ob Izmenenii Grazhdanskogo Kodeksa RSFSR, *SU* (1931), no.72, item 509) leaving its legal status to be governed by the 1927 Joint-Stock Societies Statute. During the 1920s sections 1-4 of Chapter X were also amended, but not quite so extensively.

<sup>321</sup> M.V.Gordon, *Leksii po Sovetskому Grazhdanskomu Pravu, Chast' Vtoraya* (Izdatel'stvo Khar'kovskogo Universiteta:1960), p.237.



were dead letter, there was one type of partnership that did survive the 1930s, albeit in a very different role - the simple partnership.<sup>322</sup>

#### 4.2 Background - 1961 FPCivL and the Civil Codes: The Contract for Joint Activity

Most of the Chapter X partnerships were replaced in functional terms by the introduction of the new socialist industrial organisations based on the confirmation model. By contrast, the simple partnership still retained a possible role in the new Stalin economic settlement by providing a method by which these socialist organisations could co-operate for the achievement of specific common goals.<sup>323</sup> Although instances of such cooperation were more prevalent in the agrarian economy, the simple partnership continued to be acknowledged by civil law as a legitimate form of association: "whereas the simple partnership still has some examples in everyday life, the norms of the [1922 RSFSR] Civil Code, devoted to the other types of partnership (the full partnership, the partnership on belief, the partnership with limited responsibility and the joint-stock society) on the whole lost any significance."<sup>324</sup>

In 1961, the 1922 RSFSR Civil Code was replaced as the primary framework for civil law by the all-union 1961 FPCivL which set out the general principles of civil legislation. On the basis of the 1961 FPCivL, each union republic adopted its own civil code with more detailed provisions.<sup>325</sup> The 1961 FPCivL contained no references to any of the partnerships detailed in Chapter X of the old 1922 RSFSR Civil Code. The general regulation of juridical persons was set out in brief in Section 1 of the 1961 FPCivL entitled "General Provisions",<sup>326</sup> but no mention was made of partnerships or other juridical persons in the section on the "Law of Obligations" where the provisions of the old Chapter X were found in the former 1922 RSFSR Civil Code. This might have indicated the regime's desire to remove the old then defunct provisions of Chapter X from the main framework of civil law, or more conceptually, may have been used to indicate that the theoretical basis of juridical persons was no longer to be linked to the law of obligations (ie contract).

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<sup>322</sup> There were very exceptional instances where state joint-stock societies continued to exist, operating on the basis of 1927 Statute; for example the state organisation "Inturist" (responsible for tourism in the USSR).

<sup>323</sup> This continued on the basis of the Decree, Ob Uchastii Gosudarstvennikh Uchrezhdenii i Predpriyatii v Prostoykh Tovarishchestvakh, *SU* (1926), no.29, item 184.

<sup>324</sup> *Sovetskoe Grazhdanskoe Pravo, Tom II* (Gosyurizdat:1961), p.364.

<sup>325</sup> See supra Section 2.1.

<sup>326</sup> The 1922 RSFSR Civil Code also contained general provisions relating to juridical persons in Chapter II of the "General Part".



The civil codes of each of the union republics adopted during the early 1960s on the basis of the 1961 FPCivL also did not refer explicitly to any of the old Chapter X partnerships. They did however contain provisions relating to an apparently new type of contractual relationship that was not referred to at all in the 1961 FPCivL, or by name in the old Chapter X. This was the Contract for Joint Activity.<sup>327</sup> The chapter of the union republics' civil codes of the 1960s on "Joint Activity" was contained in the sub-section of the codes on "Specific Types of Obligations". This chapter contained five articles and its wording in the code was almost identical. However, the substance of this "new" contract for joint activity revealed that it was a type of association that was identical to the old "simple partnership" - the change had been almost entirely one of terminology.<sup>328</sup>

The restructuring of the economy in the early 1960s led to a more diverse approach to economic management, and once again, joint activity was seen as a mechanism by which the, now socialist, enterprises could be encouraged to construct buildings for social purposes and work together for mutual gain. A number of pieces of legislation were enacted over the next ten years that contemplated "joint operations" by Soviet organisations. References in this legislation to acting "jointly" and "joint operations" seemed to presuppose that the legal basis for such co-operation was the contract for joint activity,<sup>329</sup> although this was rarely mentioned specifically.

The first was a decree passed in August 1964 allowing for the funds of enterprises to be joined in order to construct "objects of cultural-domestic designation, health-protection and communal economy".<sup>330</sup> This was seen as a way to ease the pressures on the central state budget. Subsequent legislation expanded on this right. The Enterprise Statute explicitly provided for the right of enterprises "to join with other enterprises and organisations the assets of the fund of the enterprise and other special assets, at its disposal, for joint (in the procedure of participatory share participation) construction of residential houses, medical and child pre-school institutions, pioneer camps and other objects of cultural-domestic designation."<sup>331</sup> A similar provision was included in the decree "On Perfecting Planning and Strengthening the

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<sup>327</sup> RSFSR CC, chapter 38.

<sup>328</sup> This was akin to the change in terminology from the artel partnership to the simple partnership made thirty years earlier when the 1922 RSFSR Civil Code itself was adopted.

<sup>329</sup> This inference was made particularly due to the use in these contexts of the term "participatory share participation" ("*dolevoe uchastie*") which was the hallmark of this type of association.

<sup>330</sup> O Stroitel'stve Ob''ektov Kul'turno-bytovogo Naznacheniya, Zdravookhraneniya i Kommunal'nogo Khozyaistva za Schet Netsentralizovannikh Istochnikov Finansirovaniya i Assignovanii, Vydelennikh na eti Tseli po Gosudarstvennomu Planu, 16 *SDZ SSSR* 544 (article 1).

<sup>331</sup> Enterprise Statute, article 56.



Economic Stimulation of Industrial Production", passed on the same day.<sup>332</sup> Joint operations were further contemplated in the 1974 Production Association Statute which provided that the construction of residential homes, communal apartments, schools and medical facilities for children, pioneer camps and other such objects of cultural-domestic designation may be carried out "jointly".<sup>333</sup>

#### 4.3 The Legacy - A Contract-based Association without Juridical Personality

The significance and history of the contract for joint activity, as developed in this Chapter, was generally ignored by Soviet civil law literature. The Soviet regime may have been anxious to rewrite the history of this form of contract in light of the fact that it constituted the only pre-revolutionary form of association to survive the recodification of Soviet civil law in 1961. For despite the fact that the contract for joint activity had a different name and function, in purely legal terms, it was almost identical to the simple partnership, and the artel partnership which preceded it.

By changing the name of this type of association once again (from simple partnership to the contract for joint activity), by removing all references to partnerships in the new 1961 FPCivL and civil codes, and by making no reference at all to this contract for joint activity in the new 1961 FPCivL, it seems that there was an attempt to de-emphasise its importance and re-characterise its significance. In one of the few references to its "true" history in Soviet legal literature, Ioffe, in his definitive study on the "Law of Obligations", noted, albeit almost in passing, that: "in the course of the liquidation of the private-capitalist economic structure and the establishment of the unrivalled supremacy of the socialist system of economy, the norms of the [1922 RSFSR] Civil Code relating to the above-listed types of partnership [ie full partnership, partnership on belief partnership with limited responsibility and joint-stock partnership] ceased to have any effect in practice. However the Civil Code also provided for the contract of simple partnership for the achievement of aims which are now served by the contract for joint activity."<sup>334</sup>

In addition to its general historical significance, from the perspective of the development of the law on industrial organisations, the contract for joint activity provided the bare conceptual and legal framework for the elaboration of the new forms of industrial organisation introduced

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<sup>332</sup> O Sovershenstvovanii Planirovaniya i Usilenii Ekonomicheskogo Stimulirovaniya Promyshlennogo Proizvodstva, 4 SDZ SSSR 5 (article 15).

<sup>333</sup> Production Association Statute, article 91. See, *Kommentarii k Polozheniyu o Proizvodstvennom Ob''edinenii (Kombinate)* (Yuridicheskaya Literatura:1979), p.160.

<sup>334</sup> O.S.Ioffe, *Obyazatel'stvennoe Pravo* (Yuridicheskaya Literatura:1975), p.765.



during the *perestroika* era. It stressed "contracting" between participants,<sup>335</sup> the concept of legislation as providing default rules,<sup>336</sup> and the principle of personal participation.<sup>337</sup> In addition, the contract for joint activity provided the theoretical link with the Soviet collective farm structures which were introduced directly into the industrial sector with the adoption of the 1988 Cooperatives Law.<sup>338</sup> While the confirmation enterprise was rooted in the socialist theories of juridical personality and state ownership, the simple partnership (or contract for joint activity), characterised merely as a type of contract, rather than a form of organisation (albeit without juridical personality), remained relatively "untainted" by these debates and Marxist doctrines.

Pre-revolutionary and Chapter X partnerships comprising juridical persons were clearly understood in terms of contract-based organisations, and therefore were contained within the civil law of obligations. By contrast, orthodox Soviet legal theory introduced the socialist concept of "forms of ownership" and re-conceptualised juridical personality within the "general" provisions of civil law by reference to the law on ownership. The contract-based rationale for juridical personality disappeared within a Soviet economic system based on state ownership of the means of production and central planning.<sup>339</sup> As has been argued, juridical personality was used to fashion an organisation capable of remaining in state ownership and of acting as the addressee of the state plan, while at the same time operating on the basis of *khozraschet* with a separate balance sheet.<sup>340</sup>

However, a contract-based association did survive this socialist ideological revolution. As described above, the contract for joint activity was considered still to have a role within the new Stalin command economy. Furthermore, there was little need to change its *legal* characterisation. Under the previous legislation the simple partnership did not give rise to a juridical person and therefore this form of association could be marginalised within the Soviet civil law of obligations without presenting a theoretical problem to the new Soviet understanding of juridical personality.

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<sup>335</sup> A principle that was developed in particular in the context of joint enterprises (infra Chapter 5) and leased enterprises (infra Section 6.5).

<sup>336</sup> While this principle became more developed after 1990 (which falls beyond the scope of this study), the coercive law governance principle began to give way to a more "permissive regime" with the introduction of the participation enterprises (infra Chapter 6) and was formalised in the 1990 Ownership Law (infra Section 7.4.1).

<sup>337</sup> The principle of participation was latent in all of the new industrial organisations of the *perestroika* period to 1990 but was the cornerstone of the "participation model" developed infra Chapter 6.

<sup>338</sup> Infra Section 6.1.3.

<sup>339</sup> Infra Section 7.4.2.1.



In common with the simple partnership, the contract for joint activity had the following legal characteristics: (i) formation on the basis of the general law of contract; (ii) personal participation and management based on the provisions of the contract; (iii) a system of legal regulation based on default rules; and (iv) property in common ownership.

But while the substance of the legislation remained unchanged, the contract for joint activity bore little *functional* resemblance to the pre-revolutionary artel partnership or the NEP-era simple partnerships. And perhaps the change of name, from simple partnership to contract for joint activity, was aimed at highlighting this change in function: the artel trade partnership and early simple partnerships were essentially associations developed as a result of negotiation and the elaboration of a common ground for activity between two independent set of interests represented by private actors doing business in the economic marketplace. By contrast, the Soviet concept of joint activity between socialist organisations was situated within the strict formal and informal governance regimes of all Soviet economic arrangements. As a practical matter, there was little negotiation of the contract itself as both participants were generally "controlled" by the same entity, the state; and it was the state that determined the extent to which co-operation for the achievement of mutual goals was necessary. As a consequence, the Soviet law on the contract for joint activity was very brief and in some cases confusing - the need for an elaborate legal framework is of course less important when, due to extra-legal control mechanisms, parties contract on the basis of diktat rather than "real" negotiation.

Despite the fact that the contract for joint activity was in practice simply another tool in the hands of the economic planners, its mere presence was of immense importance; for deep in the detail of the Soviet civil law of contract lay the seeds of a contract-based association, inherited from pre-revolutionary times, in an almost identical legal form.

#### 4.4 Formation and Participants

The contract for joint activity, like the simple partnership, was expressed to be a "contract-based" form of co-operation. The change of name to the "contract for joint activity" left the question of its nature beyond doubt. Under Soviet law a contract arose upon "reaching agreement as to all its essential points".<sup>341</sup> Despite the legal niceties which may have suggested a contract law based on *volus*, the conclusion of contracts for joint activity must be understood within the context of the Stalin economic settlement. For in economic terms, joint activity was

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<sup>340</sup> Supra Section 3.1.

<sup>341</sup> 1961 FPCivL, article 34; RSFSR CC, article 160. In common with civil law systems, Soviet contract law had no doctrine of consideration (see Arthur Taylor von Mehren and James Russell Gordley, *The Civil Law System* (Little, Brown and Company:1977), section 13).



most significantly carried out by actors within the command economy. In a command economy, the decision to contract had little to do with autonomous subjects of civil law guided by the "invisible hand". After all, private ownership had been abolished in the early years of the Soviet regime and was viewed as a bourgeois tool which facilitated exploitation of the proletariat. In general, "contracts had as their purpose the consolidation of the respective parts of the national-economic plan and the ensuring of the fulfilment of the plan";<sup>342</sup> and the requirement to contract was usually guided by the "visible hand"<sup>343</sup> of the state, either through the adoption of general plans with obligatory economic contracts,<sup>344</sup> or, more specifically, through other governance techniques described within the confirmation model.<sup>345</sup> As Ioffe and Maggs ironically noted "planning had become so detailed that there was nothing about which to contract at all".<sup>346</sup> In short, this form of contractual association was rarely the result of hard and genuine negotiation between two independent parties, but an arrangement required to be entered into at the ultimate behest of the Soviet state.

Soviet law characterised the contract for joint activity as "consensual", not simply because it was contract based, but because it was defined in the civil codes as a contract entered into for the "achievement of a common goal". This "consensual contract" was distinguished from the "creditor-debtor" relationship arising out of a contract based on "exchange". Reasoning from this Soviet notion of "consensuality", Ioffe argued that therefore the parties to a contract for joint activity were known as "participants" ("*uchastniki*") instead of the "debtor" and the "creditor".<sup>347</sup> This seems an unlikely explanation for the terminology, particularly because there is of course nothing *per se* more consensual about negotiating the terms of a joint activity agreement than the terms of a loan agreement. There are perhaps other more plausible alternative explanations: The use of the term participant may have been an attempt to move away from the language used in the 1922 RSFSR Civil Code (which used the term "partner" ("*tovarishch*")), in the same way as the name of the contract itself was changed from "simple partnership" to "joint activity". Alternatively the use of the term participant may have been due to the fact that the law of common ownership governed this type of association;<sup>348</sup> and

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<sup>342</sup> Prof.I.B.Novitskii, Prof.L.A.Lunts, *Obshchee Uchenie ob Obyazatel'stve* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1950), p.95.

<sup>343</sup> To borrow the famous pun of Alfred D. Chandler, Jr..

<sup>344</sup> 1961 FPCivL, article 33; RSFSR CC, article 159. See, V.N.Mozheiko, *Khozyaistvennyi Dogovor v SSSR* (Gosyurizdat:1962).

<sup>345</sup> See supra Section 3.4.

<sup>346</sup> Supra n.172, p.139.

<sup>347</sup> Supra n.123 (1988), p.298.

<sup>348</sup> Supra Section 2.6 and infra Section 4.6.



because the section of the civil codes regulating "common ownership" referred to each of the common owners as "participants".<sup>349</sup> The reference to the term "participant" could have been used to stress the underlying concept of "personal participation" that was the basis for this type of association. Finally, the change from the term "partner" to "participant" may have been made to highlight the fact that this form of co-operation was now to be available not just for cooperation between natural persons (ie partners) but also between juridical persons.

While the old Chapter X was silent on the point as to whether juridical persons could participate in the simple partnership, needing an explanation of the Supreme Court to settle the position,<sup>350</sup> the new provisions of the 1960s civil codes specified that both citizens and juridical persons could be participants, however the contracts could not be mixed (ie formed between citizens and juridical persons).<sup>351</sup> Indeed, as described above, after the enactment of the 1961 FPCivL and the restructuring of the economy in the 1960s, subordinate legislation frequently referred to organisations acting "jointly".

#### 4.5 Charter and Termination

A charter was a feature of a juridical person and was required to include certain basic information which in part was aimed at reinforcing the Soviet system of enterprise governance through the general civil law of *vires*.<sup>352</sup> Mainstream Soviet law characterised the contract for joint activity merely as a type of contract that did not constitute a juridical person,<sup>353</sup> and the question of a governance regime was probably overlooked and considered as simply not relevant (particularly in view of the fact that each of the participants themselves would usually have been in any event subject to state control either directly or indirectly). Therefore the civil codes did not expressly include the concept of "a charter" for the association based on the contract for joint activity. They did however set out a few limited requirements as to the *procedure* for concluding the contract (primarily that they had to be in writing),<sup>354</sup> but there were no mandatory requirements as to its content.<sup>355</sup>

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<sup>349</sup> The use of the term "participant" with respect to common ownership can be traced directly to the 1922 RSFSR Civil Code, article 63.

<sup>350</sup> Supra n.318.

<sup>351</sup> RSFSR CC, article 434. This distinction between contracts between citizens and between juridical persons was also present in the law of common ownership upon which the contract for joint activity was based (see supra Section 2.6).

<sup>352</sup> Supra Section 3.4.1.

<sup>353</sup> Infra Section 4.6.

<sup>354</sup> RSFSR CC, article 44.

<sup>355</sup> An exception to this general position was the requirement that joint activity between citizens had to be carried out with the aim of "satisfaction of their personal domestic needs" (RSFSR CC, article 434).



As the contract was by definition "for the achievement of a common economic purpose", legal practice was in any event to include in the contract a precise description of the purpose for which the association had been entered into. It was unclear as to how specific or even how necessary such a purpose clause had to be. Would the purpose of simply generating cash revenue have been sufficient? Laasik, the Estonian Soviet civil law jurist, argued that the contract should have specified not only the exact activities but also those obligations assumed by each of the participants.<sup>356</sup> Of course, due to the brevity of the default rules in the civil codes, genuine co-operation by way of joint activity based on purely legal criteria could only have been possible where the terms of the actual contract itself were relatively detailed.

In contrast to the provisions of Chapter X, there were no articles of the civil codes relating to the termination of the joint activity. This omission in the legislation was presumably part of the attempt to recharacterise this arrangement as a mere "contract" as opposed to a method for creating a permanent "organisation". Termination of the contract for joint activity was therefore governed simply by the ordinary law of contract.<sup>357</sup>

#### 4.6 Juridical Personality - Ownership Interests, *Vires* and Responsibility

The question of juridical personality (ownership, *vires* and responsibility) should have been relatively straightforward: as part of the 1960s recodification of Soviet civil law, all references to juridical persons were removed from the section of the civil codes on the law of obligations and a "new" contract, the contract for joint activity, was included in that section. This contract for joint activity should therefore have been understood simply as a contract that did not give rise to a juridical person in its own right; property contributed by the participants therefore should have remained in their ownership combined by way of common ownership; *vires* should therefore have been irrelevant as no separate juridical person was created; and responsibility should therefore have been a matter for the mainstream Soviet law of obligations where the law would "look through" the association and fix rights and obligations upon the individual participants.

However, the question of the juridical status of the contract for joint activity was a matter of some uncertainty, primarily due to the existence of inter-collective farm organisations which

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<sup>356</sup> Endel' Laasik, *Sovetskoe Grazhdanskoe Pravo, Chast' Osobennaya* (Valgus:1980), p.387.

<sup>357</sup> Most Soviet textbooks explained that this contract came to an end when the purpose of the joint activity had been achieved, or became impossible; or when there was a reorganisation of one of the participants, in the case of a juridical person, or death, in the case of a natural person (*Sovetskoe Grazhdanskoe Pravo, Chast'II* (Izdatel'stvo Yuridicheskaya Literatura:1987), p.374-5). In addition, termination could have occurred upon agreement of the parties in accordance with prevailing Soviet contract law. This formulation in the textbooks bore a remarkable similarity to the express provisions of Chapter X on termination of simple partnerships (*supra* n.317).



were juridical persons,<sup>358</sup> and were created by a contract (and a charter) between existing juridical persons for the purpose of collaborative activities;<sup>359</sup> and hence had certain theoretical similarities with the contract for joint activity. Furthermore, the articles of the civil codes regulating the contract for joint activity specifically referred to inter-collective farm organisations.<sup>360</sup>

Before the recodification of civil law in the 1960s it was relatively clear that simple partnerships were different from inter-collective farm organisations: first, only citizens (ie natural persons) could have been members of simple partnerships (whereas inter-collective farm organisations had collective farms (ie juridical persons) as members); and secondly, doctrine had become relatively settled, and the simple partnership was considered not to give rise to a juridical person, (and the inter-collective farm organisation was a juridical person<sup>361</sup>).

In fact, there were generally no references to inter-collective farm organisations in sections of Soviet civil law textbooks dealing with the nature of the simple partnership.<sup>362</sup> One exception was Ioffe's books. First, he referred explicitly to the term "contract for joint activity" before the recodification of Soviet civil law, despite the fact that this term did not appear in the Soviet primary civil law legislation of the time.<sup>363</sup> Secondly, Ioffe understood "the contract for joint activity" as an umbrella term to encompass the simple partnership contract *and* the contract for inter-collective farm activity. These two contracts were then distinguished on the basis that the simple partnership contract did not give rise to a juridical person and could be concluded between citizens, whereas the inter-collective farm contract did give rise to a juridical person and could only be concluded between juridical persons.

Ioffe in his works after the adoption of the 1960s civil codes still retained this understanding of the "contract of joint activity" (now present in the civil codes) as encompassing contract based cooperative associations between natural persons (previously simple partnerships) which

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<sup>358</sup> See RSFSR CC, article 24.

<sup>359</sup> Supra n.120, chapter VIII.

<sup>360</sup> RSFSR CC, article 434: "Under the contract for joint activity, parties shall be obliged to act jointly for the achievement of a common economic purpose: such as the construction and exploitation of inter-collective farm or state-collective farm enterprises..."

<sup>361</sup> As Gordon argued in 1960 with respect to inter-collective farms: "these associations of a new type differ from simple partnerships in that they are juridical persons and simple partnerships under the civil code do not enjoy these rights," (supra n.321, p.240).

<sup>362</sup> See, for example, *Sovetskoe Grazhdanskoe Pravo, Tom 2* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1951), pp.283-285.

<sup>363</sup> O.S.Ioffe, *Sovetskoe Grazhdanskoe Pravo II* (Izdatel'stvo Leningradskogo Universiteta:1961), pp.454-469.



did not give rise to a juridical person, *and* "inter-collective farm organisations" between juridical persons which did.<sup>364</sup> This understanding was developed from the drafting of the new RSFSR CC. In contrast to the previous articles on the simple partnership in the 1922 RSFSR Civil Code, article 434 of the new RSFSR CC directly contemplated the existence of inter-collective farm organisations within the contract for joint activity; and also permitted juridical persons (as well as citizens) to be participants in the contract for joint activity (but precluded mixed forms of contract between citizens and natural persons). This analysis seemed also to be supported by article 438 of the RSFSR CC which provided that the Council of Ministers of the union republics had the right, on the basis of the general rules, to promulgate "rules concerning individual types of joint activity";<sup>365</sup> and some commentaries and textbooks<sup>366</sup> regarded the General Statute on the Inter-Economic Enterprise (Organisation) in Agriculture as a special type of contract for joint activity, resulting in the establishment of a juridical person, adopted on the basis of this article.<sup>367</sup>

Despite the analysis presented by Ioffe, the more orthodox understanding was that the conclusion of a contract for joint activity, whether between citizens or juridical persons, precluded the creation of an association that could be recognised as an independent juridical person. Laasik explained: "when associating two or more persons on the basis of a contract for joint activity...a new subject, a juridical person, does not arise...But if the associated persons form a juridical person, the contract for joint activity may not be used to regulate the assets."<sup>368</sup> The inter-collective farm organisation was simply just a different type of association. Thus Kalandadze distinguished between agreements between collective farms regulated by the civil codes ("civil-legal agreements" (ie contracts for joint activity)) and those made on the basis of constitutive contracts for the creation of inter-collective farm

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<sup>364</sup> Supra n.334, p.769, and supra n.123 (1988), pp.298-301.

<sup>365</sup> RSFSR CC, article 438.

<sup>366</sup> *Sovetskoe Grazhdanskoe Pravo, Chast' 2* (Izdatel'stvo Leningradskogo Universiteta:1982), p.287.

<sup>367</sup> Opinion however was divided. A 1982 Commentary to the RSFSR CC noted that the General Statute on Inter-Economic Enterprises (Organisations) in Agriculture (*Obshchee Polozhenie o Mezkhkhozyaistvennom Predpriyatii (Organizatsii) v Sel'skom Khozyaistve*, 53 *SDZ SSSR* 57) was adopted on the basis of article 438. As such, the 1982 Commentary thereby acknowledged that the contract for joint activity could give rise to a juridical person (supra n.244, p.513).

Article 438 only contemplated union-republic (ie RSFSR) legislation being adopted on the basis of its provisions, and the General Statute was a piece of all-union legislation and therefore did not strictly fall within the ambit of article 438. This conclusion seemed to contradict a literal reading of article 438.

By contrast, a 1988 Commentary to the Kaz CC on the equivalent article noted that no decrees of the Cabinet of Ministers of the Kazakh SSR had been adopted pursuant to this article and did not refer to the General Statute as a source for the creation of contracts of joint activity giving rise to a juridical person (supra n.250, p.486).

<sup>368</sup> Supra n.356, pp.386-387.



organisations governed by "Model Charters" and other collective farm legislation ("inter-collective farm-legal agreements").<sup>369</sup>

Collective farm (as opposed to civil) legislation also made this distinction between (i) joint activity between collective farms without the formation of a juridical person, conceptualised within the terms of the contract for joint activity,<sup>370</sup> and (ii) co-operation between collective farms leading to the creation of separate inter-collective farm juridical persons.<sup>371</sup> As one civil law textbook explained: "if inter-collective farm enterprises or organisations are provided with the rights of a juridical person, their activities shall be regulated by the corresponding charter or statute and not by a contract for joint activity."<sup>372</sup>

This orthodox understanding was also consistent with the approach to the ownership regime for the participants as set out in the provisions of the RSFSR CC. Similar to the articles on the simple partnership in the former 1922 RSFSR Civil Code, the RSFSR CC adopted expressly the regime of "common ownership" ("*obshchei sobstvennost'yu*") for the contract for joint activity, whereby participants contributed fees ("*vznosy*") to "common property" in which participants had participatory shares ("*dolei*").<sup>373</sup> This property was used to cover losses and obligations; and if not sufficient, in the absence of a different procedure specified in the contract, outstanding debts would be divided between the participants "proportionately to their fees" to the common property.<sup>374</sup>

Unfortunately, as with the question of juridical status, the reference to operations on the basis of "common ownership" was also not free from ambiguity. In particular, certain aspects of the provisions of the civil codes on common share ownership generally<sup>375</sup> seemed to contradict corresponding specific provisions on the contract for joint activity. For example, the law of common ownership allowed for the right of any participant to require the separation out of its property; whereas the articles of the civil code on joint activity only allowed for "disposition

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<sup>369</sup> A.M.Kalandadze, *Pravovie Formi Khozyaustvennoi Deyatel'nosti Kolkhozov* (Gosyurizdat:1959), p.95.

<sup>370</sup> The 1967 Collective Farm Charter (article 19) allowed collective farms to "join part of its assets with assets of local Soviets of deputies of the workers, collective farms and other state and cooperative enterprises and organisations for the construction, on participatory principles, of objects of cultural-domestic designation...".

<sup>371</sup> In fact the "intercollective farm organisation" as a juridical person was explicitly provided for in article 11 of the 1961 FPCivL and the corresponding provisions of the civil codes, and the "contract for joint activity" was not.

<sup>372</sup> *Grazhdanskoe Pravo Kazakhskoi SSR, Chast' II* (Izdatel'stvo Mektep:1980), p.228. For the orthodox position generally on inter-economic organisations see, *supra* n.41 (1986), pp.154-158.

<sup>373</sup> RSFSR CC, article 436.

<sup>374</sup> RSFSR CC, article 437.

<sup>375</sup> RSFSR CC, article 116 *et seq.*



of its participatory share" with the consent of all the remaining participants; and the law of common ownership provided that expenses relating to the property were to be paid proportionally to the participants' "fees" in the common property; whereas provisions of the civil code specifically on joint activity stipulated that the actual provisions of the contract could provide otherwise.

The uncertain nature of the property relations and juridical status of the contract for joint activity can be traced to the law of its predecessor, the simple partnership: both avoided a clear statement that no juridical person was created; both resulted in the general understanding that no juridical person was created; and both provided for a property regime based on common ownership. However this was confused: In the case of the simple partnership this was as a result of the introduction of the concept of the reified partnership and inconsistent terminology; and in the case of the contract for joint activity this was as a result of direct references in the section of the civil codes on joint activity to the inter-collective farm organisations (which were juridical persons), and furthermore, due to the contradictions between that section and the general law on common ownership.

While Shershenevich had expressly acknowledged the ambiguities in the legislation on the artel partnership of pre-revolutionary law, civil law textbooks of the Soviet period generally adopted one of the interpretations and presented it as free from doubt. There was almost no acknowledgement that there may even have been any room for discussion on these issues and certainly no textbook framed the debate in the terms presented in this Section 3.6 and in this Chapter 3 generally.

Once again, this lack of appreciation of the ambiguities latent in the legislation may have been due to the fact that Soviet law did not have a developed concept of the ownership interest, preferring instead to finesse some of the finer points of the distinctions raised while pursuing the development of a regime based on forms of ownership.<sup>376</sup> The legislation on the bridge merely reaffirmed an existing approach to ownership interests that resulted in a law sufficiently developed for a quasi-feudal state ownership regime based on Marxist legal theory, but hopelessly ill-prepared for the *perestroika* economy where state ownership was to give way to the possibility of separate interests and fragmental ownership.

#### 4.7 Management

The provisions of the civil codes relating to the management of the activities of the participants in the contract for joint activity were relatively brief and were once again

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See *supra* Section 2.5.



inherited from the law on simple partnerships set out in Chapter X. In short, business was to be conducted by the "common consent" of the participants; however, the participants had the right to empower through a power of attorney "one of the participants" to carry out the general business and administration of the joint activity on behalf of the others.<sup>377</sup>

The requirement for unanimity was not subject to any qualification, as had been the case under Chapter X where majority voting was permitted in the simple partnership to the extent contemplated in the constitutive contract. However the empowerment of one of the participants as a sort of managing director did enable a streamlining of operations within the limits of delegated competences as set out in the power of attorney. The unanimity requirement can perhaps be viewed again as a result of the philosophy of personal participation and joint endeavour through complete mutuality of interest. In such a regime, there was no room for dissent or majority decision making. Furthermore there was no possibility for separate management organs of participants and directors. To this extent the bridge presented a rather rudimentary governance framework.

#### 4.8 Conclusion

The simple partnership became the contract for joint activity with the 1960s civil law reform and adoption of civil codes. Despite the fact that it specifically contemplated juridical persons, as well as citizens, acting as participants, this association was generally regarded as not giving rise to a juridical person. Joint activity was conceptualised purely in terms of the Soviet law of obligations providing a basic contractual mechanism for associating in order to carry out a common specific purpose by pooling resources.

It is perhaps for this reason that, while the contract for joint activity was clearly a form of association, Soviet civil law never explicitly classified the contract for joint activity together with the forms of organisation which constituted juridical persons. As such, the contract for joint activity avoided much of the ideological baggage that was constantly associated with socialist juridical persons and their rationale. For while Venediktov and his successors developed the theory of the Soviet industrial juridical person based on the concept of state ownership, they failed to take into account the position of the remaining form of association that was contract-based and was not a juridical person.

Therefore the contract for joint activity remained, hidden deep within the Soviet civil codes, classified within the law of obligations - the only form of association that was capable of bridging all the major upheavals in Russian law from pre-revolutionary times to the present

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RSFSR CC, article 435.



day. For although both its name and function changed, its legal basis remained broadly untouched. So throughout the Soviet period, there persisted in the civil codes a form of association that would become the seed of destruction for the theory of the socialist industrial organisation, budding and blooming into a contract-based association, based on personal participation and regulated by default rules: an "association" that would form the basis for new "organisations" (ie juridical persons) that would eventually usurp the position of the traditional socialist forms and herald in a new ideology of the juridical person based on *volus*, contract and the market.

The presence of the bridge explains why the introduction of the "joint enterprise" during the *perestroika* years should not have been regarded with surprise.<sup>378</sup> At the time of its introduction, the joint enterprise was regarded as a wholly "new" organisational form introduced into the area of foreign relations law. However, that understanding ignored the fact that there was an existing associational form within the Soviet law of obligations, operating alongside the confirmation enterprises, that also was contract-based. Therefore, the joint enterprise and the other new organisations of the *perestroika* era based on contract did not represent a total break from the traditional Soviet civil law of associations understood in its broadest sense. For it was the contract for joint activity that provided the historical and conceptual bridge between the model of the confirmation enterprise and the model of the contract-based concession enterprise - between the command economy and the market-orientated economy.

The legacy of the contract for joint activity however was more specific and more pervasive: not only did it incubate within Soviet law an association governed by contract, but it also preserved the role of personal participation, a permissive law based on the right to "contract out" of default rules. Finally, there was an ownership framework that was decidedly ambiguous. And all of these elements carried through the legislation from the joint enterprises to the participation enterprises which followed them and became key points of principle in the new economic constitution that emerged in the Spring of 1990.

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See *infra* Chapter 5.



## 5. MODEL 2 - THE CONTRACT-BASED CONCESSION ENTERPRISE: 1987 JOINT ENTERPRISES

*"We had adopted an essentially piecemeal strategy that tackled isolated problems without providing a comprehensive solution. Moreover, some of these measures bore the stamp of traditional methods and eventually had to be abandoned."*

Mikhail S. Gorbachev

The joint enterprise was a contract-based concession enterprise which operated on the basis of legislation adopted in January 1987.<sup>379</sup> Under Decree 49, as it was known, firms of capitalist and developing countries were permitted to establish, jointly with Soviet organisations, a Soviet juridical person created for the achievement of certain economic goals. As with many of the *perestroika* era legislative enactments, Decree 49 only had significance in practice for a limited period of time, after which it became anachronistic and was replaced by subsequent legislation. By the end of 1990, after the adoption of new legislation in the areas of foreign relations and civil law, new forms of investment vehicles were permitted to be created in the

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<sup>379</sup> Two decrees were adopted in January 1987, commonly referred to as Decree 48 and Decree 49. Decree 48 provided for the establishment of joint economic organisations (being joint enterprises, international associations and joint organisations (on the differences between these forms, see infra n.403) with members of SEV); and Decree 49 provided for the establishment of joint enterprises with firms of capitalist and developing countries: O Poryadke Sozdaniya na Territorii SSSR i Deyatel'nosti Sovmestnykh Predpriyatii, Mezhdunarodnykh Ob'edinenii i Organizatsii SSSR i Drugikh Stran - Chlenov SEV, *Postanovleniya* (January 1987), no.48, p.76; O Poryadke Sozdaniya na Territorii SSSR i Deyatel'nosti Sovmestnykh Predpriyatii s Uchastiem Sovetskikh Organizatsii i Firm Kapitalisticheskikh i Razvivayushchikhsya Stran, *Postanovleniya* (January 1987), no.49, p.88.

There were at least three versions of Decree 49: (i) the official published version (*SP SSSR* (1987), no.9, item 40) where article 2 consisted of three paragraphs, and article 3 of one paragraph; (ii) a second version "for internal use only" (*Postanovleniya* (January 1987), no.49, p.88) where the Russian word "*sekretno*" appeared after the second paragraph of article 2 and after the first paragraph of article 3; and (iii) a third version containing the text noted as "secret" in the second version. The author understands from discussions with employees at the Ministry of Justice in the Republics of Kazakhstan and Tadjikistan that the third version contained provisions for use by the KGB and copies of this text were only made available to the relevant agencies of that institution.

Not only did the "second version" of Decree 49 include references to "secret" provisions, but so did the decrees which amended it. For example the last paragraph of the amendments to Decree 49 annexed to Decree 385 (infra n.407) in the version "for internal use only" was also simply noted as "secret".



Soviet Union and these broadly presented more advantages than the Decree 49 joint enterprises.<sup>380</sup>

The significance of the joint enterprise in history of the foundations of the industrial organisation cannot be overstated. Despite earlier forms of association that resembled in some respects the joint enterprise,<sup>381</sup> it will be argued that Decree 49 should be viewed as a watershed in the restructuring of the law on industrial organisations in the Soviet Union: the joint enterprise was the first Soviet juridical person to emerge from Gorbachev's "new thinking" that exhibited some of the characteristics of the western-style corporation. However, the joint enterprise was schizophrenic, unsure of its legal foundation and unsure of its "corporate" identity. It was intended to operate within the sphere of foreign relations law, but in fact had its basic legal foundations in domestic Soviet civil law. Thus it straddled two branches of Soviet law which had for over fifty years been strictly separated. While straddling two branches of Soviet law, it also straddled two conceptions of the industrial organisation. The joint enterprise was formed on the basis of a concession, but operated on the basis of a contract negotiated between the parties. In order to understand the nature of the joint enterprise and its unique and pivotal role in the history of the law on industrial organisations, we shall first need to outline briefly the environment in which it arose:

The Soviet regime had flirted with the concept of joint ventures with other countries throughout its history, but rarely were such joint ventures permitted to be created on the territory of the USSR itself.<sup>382</sup> This was principally due to the fact that Soviet foreign relations law and policy was based upon a state monopoly - a principle that can be traced back to

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<sup>380</sup> The adoption in 1990 by Gorbachev of an edict that allowed for the creation of Soviet juridical persons *wholly-owned* by foreign firms removed the necessity for setting up "joint" operations (in the absence of specific considerations) (*Ob Inostrannykh Investitsiyakh v SSSR, Vedomosti SND SSSR* (1990), no.44, item 944). This edict was followed by the adoption of the 1990 FPInvA and the 1991 FPForInv (and corresponding foreign investment legislation in each of the union republics) which set out a new basis for the regulation and conduct of foreign investment; however neither of these enactments introduced a new form of association into domestic law in the way that Decrees 48 and 49 had done three years earlier. See generally, M.I.Braginskii, W.E.Butler, A.A.Rubanov, *The Butler Commentaries on Soviet Law: Fundamental Principles of Legislation on Investment Activity in the USSR and Republics* (Interlist:1991); and M.I.Braginskii, W.E.Butler, A.A.Rubanov, *The Butler Commentaries on Soviet Law: Foreign Investment Legislation in the Republics of the Former Soviet Union* (Interlist:1993).

<sup>381</sup> See for example the contract for joint activity (analysed in Chapter 4) and the 1983 joint economic organisations (see *infra* n.400 below).

<sup>382</sup> See, *infra* n.399.



1918,<sup>383</sup> and was considered to be "one of the deciding conditions for the success of socialist construction."<sup>384</sup> The most notable exception was the "concessions" of the NEP era, introduced in the early 1920s when the Soviet policy on foreign trade was still unsettled, embroiled in the debate over the relative merits of an "absolute" state monopoly as against a more "liberal" one.<sup>385</sup> Foreign investment was permitted under the Dekret on Concessions adopted in 1920,<sup>386</sup> or through the creation of "specially chartered joint-stock enterprises, Russian, Foreign and Mixed, having the purpose of attracting foreign capital."<sup>387</sup> Where mixed, the Soviet side had to hold at least 51% of the stocks.<sup>388</sup> The institutional framework for the granting of concessions was set up in 1922 in the form of the Concession Committee attached to Gosplan and the Commission for Mixed Societies attached to the Soviet of Labour and Defence. These were eventually merged in 1923 to form the Main Concession Committee attached to the USSR Council of People's Commissars.<sup>389</sup>

Soviet literature of the post-NEP era emphasised the fact that these concessions were only intended at the time to be a temporary measure and had little real significance in economic terms. In total from the period 1921 - 1926, out of 1,937 "offers" to conclude concession contracts, only 135 were in fact concluded.<sup>390</sup> By 1928 Soviet policy had in any event shifted yet again moving towards what John Quigley described as "extreme centralisation in both trade and industry";<sup>391</sup> and between 1928 - 1929 no new concessions were granted, and several were even terminated.<sup>392</sup> This change in policy was formalised by a decree of the All-Union Soviet of People's Commissars on 27 December 1930 which ended the granting of foreign concessions for mining and manufacturing.<sup>393</sup> As Pedersen writing in 1975 noted, "since that date the Soviet Union has followed a policy of prohibiting the participation by

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<sup>383</sup> O Natsionalizatsii Vneshnei Torgovli, *SU* (1918), no.33, item 432. See, *Pravovye Voprosy Vneshnei Torgovli SSSR* (Vneshtorgizdat:1955), p.6 and p.54.

<sup>384</sup> S.S.Studenkin, *Sovetskoe Administrativnoe Pravo* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1949), p.185.

<sup>385</sup> John Quigley, *The Soviet Foreign Trade Monopoly, Institutions and Laws* (Ohio State University Press:1974), p.25.

<sup>386</sup> Obshchie Ekonomicheskie i Yuridicheskie Usloviya Kontsessii, *SU* (1921), no. 91, item 181.

<sup>387</sup> O Vneshnei Torgovle, 13 Marta 1922, supra n.111 (1967), p.293.

<sup>388</sup> M.M.Boguslavskii, *Mezhdunarodnoe Chastnoe Pravo* (Mezhdunarodnye Otnosheniya:1977), p.137.

<sup>389</sup> M.M.Boguslavskii, *Inostrannye Investitsii: Pravovoe Regulirovanie* (Izdatel'stvo BEK:1996), p.5.

<sup>390</sup> Supra n.178, p.162.

<sup>391</sup> Supra n.385, p.61.

<sup>392</sup> Ibid., p.6.

<sup>393</sup> James F. Pedersen, *Joint Ventures in the Soviet Union: A Legal and Economic Perspective* (1975) 16 *Harv.International LJ* 390.



foreign firms in the management and sharing of profits in economic organisations within the USSR...Consequently there are today no economic associations in the USSR between Western firms and Soviet economic organizations involving joint management and the sharing of profits and losses".<sup>394</sup> This situation was to continue until January 1987. However, joint ventures as creatures of public international law had been in existence for a number of years prior to that date.

The Soviet policy in international relations changed radically after the death of Stalin when foreign trade increased and Comecon became a more active body.<sup>395</sup> With the opening up of the economy, the question of joint ventures was raised again and a number were established, particularly with member countries of SEV. Section 15, article 7 of The Complex Programme of SEV provided that member countries should prepare the necessary legislation to facilitate the creation of "international economic organisations" in the fields of production, trade, scientific-technological co-operation and other areas.<sup>396</sup> As a result, in January 1973, the Executive Committee of SEV adopted the "Model Statute on the Conditions for the Establishment and Activity of International Economic Organisations in the Member Countries of SEV"; in January 1975 the "Model Statute on the Financing and Effectuation of Expenses of International Organisations of the Interested Member Countries of SEV"; and in January 1976 the "Uniform Statute on the Establishment and Activity of International Economic Organisations."<sup>397</sup> Cooperation among the members of SEV increased still further after the December 1985 (Extraordinary) Meeting of the Session of SEV, and between 1986 and 1987 a number of bilateral international treaties were signed relating to the establishment of international economic organisations and setting out the basic norms for their operations.<sup>398</sup> A number of joint ventures were therefore established pursuant to these enactments. However, all of them were set up outside the Soviet Union and were only engaged in trade and fishing, never in the sphere of industry.<sup>399</sup>

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<sup>394</sup> Ibid.

<sup>395</sup> Supra n.191, p.358.

<sup>396</sup> *Osnovnye Dokumenty Soveta Ekonomicheskoi Vzaimopomoshchi, Tom 1* (Sekretariat SEV:1981), p.117.

<sup>397</sup> G.D.Golubov, *Sovmestnye Predpriyatiya Mezhdunarodnye Ob''edineniya i Organizatsii na Territorii SSSR* (Yuridicheskaya Literatura:1988), pp.14-15.

<sup>398</sup> Treaties were signed with Poland (15 October 1986), Bulgaria, Hungary and Czechoslovakia (4 November 1986) and East Germany (17 December 1986) before the adoption of Decree 48 in January of the following year. These treaties set out the basic provisions upon which co-operation would proceed and charters would be drawn up. Supra n.397, pp.536-537.

<sup>399</sup> M.M.Boguslavskii, *Joint Ventures in the Soviet Union* (I.B.Tauris & Co Ltd:1991), pp.14-15. On the role of Soviet state participation in foreign companies see, William B. Simons, *Soviet Foreign Trade: Economic, Legal and Political Aspects* in supra n.174, pp.270-75.



Building upon these developments in international cooperation, in the domestic sphere the presidium of the Supreme Soviet of the USSR passed in 1983 the Edict "On the Procedure for the Effectuation of Activities on the Territory of the USSR by Joint Economic Organisations of the USSR and other Member Countries of SEV".<sup>400</sup> Three principal points expressed in the edict should be noted: first, these "joint economic organisations" were authorised to be established on the territory of the USSR; secondly, they operated broadly on the basis of USSR legislation (other than as specifically provided for by the applicable treaties between the relevant governments and states); and finally, "their" property remained in the "common socialist ownership" of the contracting parties allocated to the joint organisation by way of "operative management". While this edict provided for the possibility of the establishment of joint ventures on the territory of the USSR for the first time since the NEP era concessions and associations, they still operated essentially within the confirmation model in that their creation was based upon the diktat of the relevant member states and the governance regime of the confirmation model applied to their operation, including the socialist concept of "operative management" and thereby continued the Soviet tradition of finessing the proper and complete analysis of the concept of ownership interests.<sup>401</sup> However this edict did re-open the debate on the structure of foreign trade and prepared the way for the reform of foreign trade institutions in 1986,<sup>402</sup> as well as the introduction of joint enterprise legislation in 1987.

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<sup>400</sup> O Poryadke Osushchestvleniya Deyatel'nosti na Territorii SSSR Sovmestnykh Khozyaistvennykh Organizatsii SSSR i Drugikh Stran - Chlenov SEV, *Vedomosti SSSR* (1983), no.22, item 330; confirmed by the Supreme Soviet (*Vedomosti SSSR* (1983), no.25, item 385). See N.V. Mironov, Pravovoi Status Sovmestnykh Khozyaistvennykh Organizatsii Stran - Chlenov SEV na Territorii SSSR, *SGiP* (1984), no.3, p.43.

<sup>401</sup> See supra Chapter 3 on the confirmation model. Despite this initiative by Andropov in 1983, there was no attempt to move the law on industrial organisations towards a more flexible contract based model. Andropov's brief tenure as General Secretary of the CPSU was more clearly identified with initiatives aimed at "strengthening control over and increasing responsibility for breaches of discipline at enterprises" and raising "the level of discipline, vigilance and intolerance" as means of improving productivity. (Mikhail Heller and Alexandr Nekrich, *Utopia in Power - the History of the Soviet Union from 1917 to the Present* (Summit Books:1986), p.709 and p.710).

<sup>402</sup> The reform of the framework of foreign trade began in August 1986 with the adoption of Decrees 991 and 992 on 19 August 1986: O Merakh po Sovershenstvovaniyu Upravleniya Vneshneekonomicheskimi Svyazi, *SP SSSR* (1986), no.33, item 172; and O Merakh po Sovershenstvovaniyu Upravleniya Ekonomicheskimi i Nauchno-tekhnicheskimi Sotrudnichestvom s Sotsialisticheskimi Stranami, *Postanovleniya* (August 1986), no.992, p.244. It is interesting to note that only the very briefest of extracts of these two decrees was published in the official *SP SSSR*, and that the chronological set of decrees "for internal use only" omitted the text of Decree 991 in its entirety. A very brief reference was subsequently made in *Izvestiya* (17 August 1986), p.1. The lack of a complete published text perhaps evidenced the sensitivity of these first tentative reforms. On the reform of foreign relations law and institutions generally, see William B. Simons, The Reform of Soviet Foreign Trade Through Perestroika: Decentralisation without Deregulation, in A.J.Schmidt (ed.), *The Impact of Perestroika on Soviet Law* (Kluwer:1990), p.387.



"Joint enterprises"<sup>403</sup> were directly introduced into domestic Soviet law in January 1987 by Decrees 48 and 49 and by an Edict of the Presidium of the Supreme Soviet passed on the same day.<sup>404</sup> Decree 49 defined joint enterprises as entities "with the participation of soviet organisations and firms of capitalist and developing countries...created on the territory of the USSR...on the basis of contracts concluded with the participants."<sup>405</sup> Their purpose was to facilitate the "further developing of trade-economic and scientific-technical cooperation with capitalist and developing countries on a stable and mutually-advantageous basis".<sup>406</sup>

Decree 49 was amended six times, most dramatically by Decree 385 of May 1989.<sup>407</sup> In addition to these amendments, the legal regulation of joint enterprises and foreign relations law was significantly affected indirectly by the adoption of the 1987 Law on Enterprises and the 1990 Ownership Law,<sup>408</sup> and more directly by the 1990 FPInvA and the 1991 FPForInv. The detail of the law on joint enterprises was further elaborated in subordinate legislation and instructions of state agencies.<sup>409</sup>

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<sup>403</sup> Strictly speaking, Decrees 48 and 49 distinguished joint enterprises, international associations and joint organisations. The joint enterprise was the only permitted form of association for creating a Soviet juridical person with the participation of firms from capitalist and developing countries. The international association could only be created with member countries of SEV and was used merely to "coordinate" the economic activity of its participants generally, without the establishment of a common property fund. The joint organisation was also only permitted to be created between member countries of SEV, but by contrast, had common property held on the basis of socialist ownership and was formed for the purpose of research rather than for economic activity.

<sup>404</sup> O Voprosakh, Svyazannykh s Sozdaniem na Territorii SSSR i Deyatel'nostyu Sovmestnykh Predpriyatii, Mezhdunarodnykh Ob''edinenii i Organizatsii s Uchastiem Sovetskikh i Inostrannykh Organizatsii, Firm i Organov Upravleniya, *Vedomosti SSSR* (1987), no.2, item 35.

<sup>405</sup> Decree 49, article 1.

<sup>406</sup> Decree 49, preamble.

<sup>407</sup> The relevant decrees being: Ob Izmenenii i Priznanii Utrativshimi Silu Reshenii Pravitel'stva SSSR v Svyazi s Sovershenstvovaniem Vneshneekonomicheskoi Deyatel'nosti, *Postanovleniya* (March 1988), no.352, p.238; Ob Izmenenii i Priznanii Utrativshimi Silu Nekotorykh Reshenii Pravitel'stva SSSR po Voprosam Vneshneekonomicheskoi Deyatel'nosti, *Postanovleniya* (May 1989), no.385, p.11; Ob Izmenenii i Priznanii Utrativshimi Silu Nekotorykh Reshenii Pravitel'stva SSSR po Voprosam Vneshneekonomicheskoi Deyatel'nosti, *Postanovleniya* (July 1989), no.574, p.99; Ob Izmenenii Utrativshimi Silu Reshenii Pravitel'stva SSSR v Svyazi s Zakonom SSSR O Podokhodnom Naloge s Grazhdan SSSR, Inostrannykh Grazhdan i Lits Bez Grazhdanstva, *Postanovleniya* (August 1990), no.780, p.37; O Vnesenii Izmenenii i Priznanii Utrativshimi Silu Nekotorykh Reshenii Pravitel'stva SSSR po Voprosam Nalogooblozheniya, *Postanovleniya* (September 1990), no.884, p.5. In addition: O Dal'neishem Razvitii Vneshneekonomicheskoi Deyatel'nosti Gosudarstvennykh, Kooperativnykh i Inykh Obshchestvennykh Predpriyatii, Ob''edinenii i Organizatsii, *Postanovleniya* (December 1988), no.1405, p.93.

<sup>408</sup> See infra Chapter 7.

<sup>409</sup> Subordinate legislative acts included Instruction of the Ministry of Finance of the USSR No 224 of 24 November 1987, O Poryadke Registratsii Sovmestnykh Predpriyatii, Mezhdunarodnykh Ob''edinenii i Organizatsii, Sozdavaemykh na Territorii SSSR s Uchastiem Sovetskikh i Inostrannykh Organizatsii,



The framework of Soviet legislation had so developed since the 1920s that by 1987 it was difficult to point to any basic provision of Soviet law that contemplated specifically the existence of "foreign-owned" Soviet civil law juridical persons. Although the provisions of Decree 49 broke new ground at the level of principle, they were not however entirely inconsistent with existing norms of Soviet law as set out in the USSR Constitution and 1961 FPCivL. The Brezhnev Constitution was silent as to the creation of Soviet juridical persons by foreign firms, and article 29 actually provided for "cooperation between states", which was then (re)interpreted as permitting cooperation by means of joint enterprise. The joint enterprise was not mentioned in the original list of permissible juridical persons in article 11 of the 1961 FPCivL; however article 11 was amended in 1981 by adding at the end of that list the phrase "...and other organisations in the instances provided by the legislation of the USSR shall be juridical persons".<sup>410</sup> As such, the joint enterprise as a domestic Soviet civil law juridical person could conveniently fall within this catch-all amendment. Unfortunately while the joint enterprise could fall within the catch-all category in the article 11 list of juridical persons, there was no "catch-all" category for the forms of ownership. As such, the ownership regime of the joint enterprise was condemned to an uncertain civil law footing and this created an instability that would eventually lead to a revaluation of the whole ownership law regime in the Spring of 1990.

### 5.1 The Model of the Contract-Based Concession Enterprise - General Principles

Soviet law distinguished the branch of civil law, from that of foreign relations law - the former related to the internal economic monopoly (regulated specifically by Gosplan and Gossnab) while the latter related to the external economic monopoly (regulated specifically by the Ministry of Foreign Trade). This bifurcated structure made some sense in the context of the Soviet command economy and was developed in response partly to historical, partly to

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Firm i Organov Upravleniya; Instructive Letter of the Ministry of Finance of the USSR and Central Statistical Administration of the USSR No 53/13-09 of 27 February 1987, O Vedenii Ucheta i Otchetnosti na Sovmestnykh Predpriyatiyakh, v Mezhdunarodnykh Ob'edineniyakh i Organizatsiyakh, Sozdavaemykh na Territorii SSSR; Instruction of the Ministry of Finance of the USSR No 124 of 4 May 1987, O Nalogooblozhenii Sovmestnykh Predpriyatii"; Decree of Gossnab of USSR No 74 of 4 June 1987, Poryadok Material'no-Tekhnicheskogo Snabzheniya Sovmestnykh Predpriyatii, Sozdavaemykh na Territorii SSSR s Uchastiem Drugikh Stran i Zarubezhnykh Firm, i Sbyta ikh Produktsii; Instruction of the Ministry of Finance of the USSR No 45-15-1 of 5 June 1987, O Poryadke Strakhovaniya Imuchestva i Interesov Sovmestnykh Predpriyatii (see *Sovmestnye Predpriyatiya, Sozdanie i Deyatel'nost'* (Lybid':1990), p.7-8).

<sup>410</sup> O Venesenii Izmenenii i Dopolnenii v Osnovy Grazhdanskogo Zakonodatel'stva Soyuza SSR i Soyuznykh Respublik, *Vedomosti SSSR* (1981), no.44, item 1184. Corresponding amendments were made to the union republic civil code provisions.



ideological, factors.<sup>411</sup> Soviet law located the joint enterprise firmly within the law of foreign relations;<sup>412</sup> and it was introduced in 1987 specifically as a vehicle for the carrying out of *foreign economic activities* in the tradition of the previous joint ventures with member countries of SEV.<sup>413</sup> The main difference from the former SEV regime usually noted was that Decree 49 permitted participants from capitalist and developing countries to form joint enterprises whereas previously joint ventures were generally only permitted to be established with organisations of member countries of SEV. Therefore many of the legal theoretical debates surrounding the nature of joint enterprise focused on private international law issues.<sup>414</sup>

The adoption of the joint enterprise into Soviet law and its "perceived" role must be understood within the context of the *perestroika* reforms. The entire legislative programme of the early *perestroika* period broadly proceeded on the basis of existing categories and branches of law, and attempted to "tinker" or amend them by *ad hoc* measures. There was initially no real attempt to reconstruct Soviet law at the level of principle and then to enact consequential reform of the positive law from the top down.<sup>415</sup> To this extent the *perestroika*

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<sup>411</sup> On the establishment of the internal monopoly see Robert Service, *A History of Twentieth Century Russia* (Allen Lane, The Penguin Press:1997), chapter 9; and on the establishment of the external monopoly see *supra* n.385.

<sup>412</sup> For example, Boguslavskii, the Soviet private international law scholar, noted that joint enterprises could be seen in three ways: (a) as a form of international economic cooperation; (b) as a form of involving foreign investment; (c); as a form of organising pertinent economic activity: *supra* n.399, p.15. There was however no mention by Boguslavskii of their role in the context of *civil law* (ie as a "new" Soviet juridical person). Consistent with this approach, Soviet civil lawyers generally made little or no mention of joint enterprises in their treatment of article 11 of the 1961 FPCivL or the development of the joint-stock society and other industrial organisations. For example, a 1993 textbook on Russian civil law contained an extensive chapter on types and classifications of juridical persons without any consideration of the joint enterprise or juridical persons with foreign participation. Where "economic associations of juridical persons" were discussed, the text limited itself to domestic "unions" and "concerns" without mentioning the possibility of forming "joint enterprises" (*Grazhdanskoe Pravo* (Izdatel'stvo BEK:1993), pp.86-107). Examples of this treatment of joint enterprises in western literature include *supra* n.34 (where joint enterprises are mentioned in the chapter on "Foreign Economic Relations" (p.272) and not in the chapter on "Enterprises" (p.257)). For exception, noting the domestic law juridical status and significance of the joint enterprise, see *supra* n.409, p.12 *et seq* and p.39 *et seq*.

<sup>413</sup> See N.N Vosnesenskaya, *Sovmestnye Predpriyatiya s Uchastiem Firm Kapitalisticheskikh i Razvivayushchikhsya Stran na Territorii SSSR*, *SGiP* (1988), no.1, p.117.

<sup>414</sup> Soviet lawyers raised a number of procedural issues relating to the constitutive documents, especially from the point of view of foreign relations law. For example, many Soviet private international lawyers argued that the constitutive contract of the joint enterprise was a "foreign-trade transaction" and thus had to be signed by two signatories from each participant in compliance with the established USSR foreign relations law rule (O Poryadke Podpisaniya Vneshnetorgovykh Sdelok, (1978) *Postanovleniya*, no.122, p.128).

<sup>415</sup> Most of the legislation of the *perestroika* period was adopted to address a specific issue by a specific enactment rather than an attempt to develop and rationalise a new set of legal principles consistent throughout all branches of Soviet law. For example, the 1990 Ownership Law was adopted to address the



reforms resembled more the "common law" organic approach to legal systemic evolution as opposed to the more holistic Romanist civil law approach.<sup>416</sup> Joint enterprises were also conceived narrowly, introduced simply as part of the reform of foreign relations law. However, the joint enterprise was a foreign investment vehicle with a difference - it was a *Soviet juridical person* and hence a subject of Soviet *domestic civil law* operating on the territory of the USSR. Unfortunately though, for as long as the Soviet regime characterised the joint enterprise narrowly as a foreign investment vehicle within the law of foreign relations, the place of the joint enterprise within the Soviet domestic economy and supply system remained ambiguous.

This Chapter attempts to reposition the place of the joint enterprise within the history of industrial organisations in the Soviet Union, Russia and the other former Soviet republics. For the significance of the joint enterprise is not really to be found by understanding it as a foreign investment initiative. In summary, Decree 49 was the first enactment perhaps since the 1920s that contemplated a truly new model of industrial organisation with an independent civil law juridical personality. Decree 49 radicalised the existing contract for joint activity, reviving its role in functional terms as initially contemplated by the simple partnership in the 1922 RSFSR Civil Code.<sup>417</sup> But the gap between the perceived role of the joint enterprise and its real significance, between its place within foreign relations law and within domestic civil law, highlights its schizophrenic nature. The joint enterprise also straddled two concepts of the industrial organisation and of juridical personality; for on the one hand it arose by virtue of a "concession" or state authorisation, while on the other hand, its operations and constitutive documents were based on the civil law of contract.

In western Europe the concession corporation was a product of, what Adam Smith called, the mercantile economy of the late nineteenth century.<sup>418</sup> The mercantile economy was not sufficiently complex to incentivise large-scale financings through private capital without state intervention. One way the state encouraged such investment in key sectors of the economy was to grant the "privilege" of limited liability or a monopoly status upon associations of

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question of relations of ownership in Soviet law, notwithstanding its provisions were inconsistent with the 1961 FPCivL which never were amended. This unsatisfactory situation was dealt with in the implementing Decree which provided in article 2 that "Until legislation of the USSR and union republics is brought into conformity with the Law of the USSR "On Ownership in the USSR", prevailing acts of legislation of the USSR and union and autonomous republics shall apply insofar as they are not contrary to this Law" (*Vedomosti SND SSSR* (1990), no.11, item 165).

<sup>416</sup> See, Gyula Eorsi, *Comparative Civil (Private) Law* (Akademiai Kiado:1979), p.542.

<sup>417</sup> Sections 4.1 and 4.2.

<sup>418</sup> See Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, Book IV, chapters I and VIII, in particular with reference to the status of the East India Company.



investors. This privilege however would not be granted without a price, and the price was that such association would only be "permitted" to carry out a specifically agreed list of activities that ensured the development of these key sectors of the economy in the mutual interests of the state and the investors.

This concept of the mercantile concession corporation provides a rationale for the pre-revolutionary Tsarist corporations. Under the Russian legislation of 1836, corporate status was granted as a privilege and each charter was negotiated and agreed with the state on a case by case basis and then adopted as a legislative state act. As has been described, for similar reasons, the Soviet regime itself flirted with the concept of the concession in the early 1920s.

In 1987 the joint enterprise reintroduced the concept of the concession: this time the privilege of juridical status was granted in order to encourage foreign capital to be invested in "further developing of trade-economic and scientific-technical cooperation...on a stable and mutually advantageous basis".<sup>419</sup> The concession approach was noted by Boguslavskii: "Western countries have introduced the normative method of founding enterprises...without prior permission, while the USSR has adopted the authorisation method."<sup>420</sup>

The concession introduced by Decree 49 should be understood as a grant to specific non-Soviet organisations of the right to form a joint enterprise with a Soviet organisation for specific purposes (as requested in the application, enshrined in the charter and agreed by the state). In this way, the Decree 49 concession gave rise to a new subject of civil law owned by third parties, and therefore, most significantly, introduced an exception to the principle of state ownership of the means of production. It was not intended however to create an exception to state control over the operation of the macro economy generally nor over state monopolies in the micro economy (such as banking and insurance activities).

The differences between the confirmation model and the contract-based concession model can best be elaborated by using the prism of "interests": the former organisation is an arena for the elaboration of a single interest (that of the state), whereas the latter is an arena for the regulation and balancing of three separate interests (that of the state, the founders and the management).

The confirmation model contemplates an organisation formed on the basis of a single interest. This therefore enables the blurring of ownership relations, management functions and governance: the state is at the same time the creator-owner of the enterprise; the property-

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<sup>419</sup> Decree 49, preamble.

<sup>420</sup> Supra n.399, p.20.



owner of the property "allocated to" the enterprise; and legal and economic sovereign.<sup>421</sup> As such, in the confirmation enterprise, there is no conflict between different interests in the ownership structure of the enterprise, for the state is the only owner; no conflict over the property of the enterprise, for the state is the only owner of its property (allocated by way of operative management); no conflict between rights to profits, for the state, being the sole owner of the enterprise, had no need to share the profits with another party;<sup>422</sup> and finally no conflict in management, for management was based on the principle of one-man management. The sole function of the governance regime therefore was to align the activities of this centralised management structure with that of the state.

The contract-based concession model is marked by a retreat by the state from its role as direct creator-owner and perhaps also from its role as property-owner. The analytical framework comprising the contract-based concession model is built upon this change in role and a rationale based on the concept of "concession" and the implicit admission in Decree 49 that the Soviet state needed to attract "foreign techniques" into the Soviet economy to ensure its continued development.<sup>423</sup> As such, the Soviet state had to ensure that joint enterprises only carried out operations that would be beneficial to the Soviet economy and hence only these joint enterprises would be permitted to be established. Unfortunately the Soviet state could not on an on-going basis monitor and direct their operations through the confirmation model governance regime or through the confirmation model ownership regime because the Soviet state was no longer the direct or sole creator and was no longer the owner of all of their property.

The state therefore had to rely in the first instance upon its remaining role as sovereign, both economic and legal. This was effected by using three principal techniques: first by specifying in the legislation a detailed authorisation procedure and thereby directly controlling which joint enterprises were permitted to be established and for what specific purposes; secondly by using its role as legal sovereign to provide for mandatory legal rules that were required to be complied with as a matter of law; and thirdly by using its role as economic sovereign: joint enterprises operated within the wider Soviet domestic economy that was otherwise ultimately

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<sup>421</sup> Supra Section 3.4.

<sup>422</sup> Indeed there was no real concept at all of "profit" in Soviet economics.

<sup>423</sup> The grounds for authorising the registration of a joint enterprise are considered further in Section 5.2.1 below.



owned and controlled by one owner, the Soviet state; and therefore their activities could be limited by virtue of the exogenous economic forces of that wider state controlled economy.<sup>424</sup>

State control was also effected indirectly in cases where the Soviet participant was state owned. In these circumstances, the state retained influence indirectly as creator-owner, through its ownership of the Soviet participant, and as property-owner because it most probably retained ownership of the property contributed to the joint enterprise by the Soviet participant.<sup>425</sup>

Although the need to protect the interests of the state was perhaps inherent in the concessionary nature of the joint enterprises, the state still had to provide the appropriate conditions in the legislation to encourage the submission by foreign persons of applications to set up joint enterprises. The principal inducement offered was the grant of the right of juridical personality and the right to operate its activities within the Soviet domestic economy but outside the scope of planning instructions. Once established, the protection of the interests of the participants (Soviet and foreign) as between themselves was ensured by the provisions of the constitutive (or founding) contract which set out their mutual rights and responsibilities. More generally, the protection of the rights of the participants as against the directorate, due to the separation of ownership from control, was ensured by the governance regime outlined in the charter.

The elements of the contract-based concession model can therefore be summarised as follows:

- (a) Protection of the interests of the state through:
  - control over purposes: the authorisation procedure.
  - control over activities: the constitutive documents, the ultra vires rule and other techniques.
  - mandatory requirements and economic sovereignty
  - indirect control through ownership of the Soviet participant.
- (b) Inducement - the nature of the concession:
  - juridical personality within the framework of civil law.
  - "full" *khozraschet*, non-subsidy and self-financing and operating outside the state plan.
  - charter privileges.
  - dispute resolution.

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<sup>424</sup> This aspect of the contract-based concession model has certain similarities with the second expression of the participation model (infra Section 6.4)



- (c) Governance - the regulation and protection of the interests of the participants and the directorate:
- the constitutive contracts.
  - the property regime.
  - the operation of the board and the directorate, and the governance regime.

Each of the above features of the contract-based concession enterprise are elaborated and analysed in the subsequent Sections of this Chapter. The term "enterprise" however is still retained for this model. Despite the explosion of interests in the contract-based concession model and its resulting differences from the confirmation model, there still remained one basic theoretical and fundamental similarity. Both the state enterprise and the joint enterprise were organisations that were defined not by reference to ownership interests that characterised the "nature" of the specific juridical person (or otherwise), but by reference to the *identity* of their owners: state enterprises were defined by reference to their ownership by the state, and joint enterprises were defined by reference to being owned jointly by Soviet and foreign participants. Soviet legislation and principle classified and analysed these vehicles not in terms of the specific nature of ownership interests, nor in terms of function, nor in terms of a governance regime, but in terms of *forms* of ownership. The traditional Soviet link between the nature of juridical personality and the nature or identity of its owner, dating back to the works of Venediktov, still remained. It is for this reason that this model has been called "the contract-based concession *enterprise*". As will be argued later in this study, the concept of corporate status can only arise within the framework of ownership interests that facilitates a liquid market for investment equity and a precise understanding of the mutual property and contractual rights and obligations between owners and the judicial person. In this way, the classification of the juridical person would be elaborated by reference, not to the identity of the owners (based on forms of ownership), but by reference to the rights and obligations that are associated with the specific ownership interests issued by it.<sup>426</sup>

Nevertheless, the contract-based concession model represents the first step in the later Soviet period towards the development of the corporation. The significance of the joint enterprise therefore lies not in the fact that it contributed to the erosion of the state monopoly of foreign trade, which it surely did; nor in the fact that it was the first time since the 1920s that Soviet organisations could form vehicles with participants from capitalist countries on the territory of the Soviet Union; which it surely was. It is argued that the "real" significance of the joint

<sup>425</sup> Infra Section 5.4.2.

<sup>426</sup> Infra Section 7.2.



enterprise was that it gave rise to a new domestic juridical person and a new subject of civil law conceived within the contract-based concession model and that the future development of Soviet and Russian "corporate" law was built upon the path cleared thereby.

## **5.2 Protection of the Interests of the State**

As has been argued, the introduction of a juridical person not wholly owned by the state entailed a reorientation of the techniques by which the state had traditionally controlled its confirmation enterprises. As its roles as "creator" and "property owner" were by definition curtailed, the state had to focus on its remaining role as "sovereign". This necessitated an elevation of the importance of law, for law is the primary tool by which a sovereign seeks to protect its position; and also an elevation of the importance of maintaining control over the planned economy, for this was the principal method by which an economic sovereign maintains its hegemonic position in the wider economy.

The protection of the interests of the state in the contract-based concession model are therefore effected by way of an elaborate authorisation procedure and legislative determinants generally which provided both mandatory requirements and ensured the continuance of state monopolies.

### **5.2.1 Control over Purposes - The Authorisation Procedure**

The purposes for which a joint enterprise was created was central to the permit-ting process. The state would only grant the concession of juridical personality to an association of founders where there was a co-incidence of interest between the founders of the joint enterprise and the state. The preamble to Decree 49 provided explicitly that joint enterprises were to be admitted into the framework of Soviet civil law "for the purpose of further developing of trade-economic and scientific-technical cooperation with capitalist and developing countries on a stable and mutually-advantageous basis". Article 3 additionally provided that Ministries, when evaluating the possibility for the creation of joint enterprises by Soviet participant enterprises within their control, should ensure that the proposed joint enterprises facilitated "the fuller satisfaction of the needs of the country for specific types of industrial products, raw materials, foodstuffs, attraction to the national economy of the USSR of progressive foreign techniques and technology, management expertise, additional material and financial resources, the development of the export base of the country and the reduction of irrational imports". By reading Decree 49 one gets an immediate sense of the realisation by the Soviet regime that autarky within the socialist world was chimerical and there was a "real need" for "foreign



techniques" to be introduced into the Soviet economy, provided that those techniques could be introduced in a controlled manner.<sup>427</sup>

With the general interests of the Soviet state stated clearly in Decree 49, the legislation went on to provide a framework for ensuring that those interests were protected. Initially this was achieved through the authorisation process. The first redaction of Decree 49 provided that the USSR Council of Ministers (ie the government) had to approve the creation of each joint enterprise.<sup>428</sup> In a move that echoed the requirement for the approval of the Tsar of each charter of pre-revolutionary joint-stock societies,<sup>429</sup> the involvement of the government of the country in the permitting process illustrated the exceptional nature of the joint enterprise and a general wariness of allowing the creation of spontaneous formations without careful consideration of the merits on a case-by-case basis.

More generally Decree 49 provided a four stage formation process: application, approval, consent and registration.<sup>430</sup> The proposal for the creation of the joint enterprise, together with the feasibility study ("TEO"),<sup>431</sup> and draft constitutive documents had to be submitted by the Soviet party to the relevant Ministry and state agencies to which it was affiliated for their approval. The TEO was particularly significant as it was the document that set out the rationale for the creation of the joint enterprise, implicitly making the argument that its activities would fall within those areas of activity that the Soviet state and economy needed foreign techniques to develop.<sup>432</sup> After approval by the relevant Ministry, the consent of the USSR government was sought. Finally, the constitutive documents had to be registered at the USSR Ministry of Finance and then published in the press.<sup>433</sup>

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<sup>427</sup> The "necessity" of attracting foreign capital into the Soviet economic system was noted at the 27<sup>th</sup> Communist Party Congress in 1986: "in modern times there is no alternative to cooperation and mutual-assistance between all states. In this manner, objective...conditions arose in which the conflict between capitalism and socialism may continue only exclusively through the forms of peaceful competition and peaceful" (*Materialy XXVII S'ezda Kommunisticheskoi Partii Sovetskogo Soyuza* (Polizdat:1986), p.65).

<sup>428</sup> Decree 49, article 2.

<sup>429</sup> Thomas C. Owen, *The Corporation under Russian Law, 1800-1917, A Study in Tsarist Economic Policy* (Cambridge University Press:1991), p.23.

<sup>430</sup> On the registration procedure see, N.N. Voznesenskaya, *Sovmestnye Predpriyatiya kak Forma Mezhdunarodnogo Ekonomicheskogo Sotrudnichestva* (Nauka:1989), pp.214-219.

<sup>431</sup> See G.D.Golubov (ed.), *Joint Ventures and International Associations in the USSR* (Intershelf:1989), p.24-28.

<sup>432</sup> On the drawing up of the TEO, see supra n.397, pp.43-49.

<sup>433</sup> Decree 49, article 9. The fact that a notice of the registration of each joint enterprise had to be published in the national press illustrated again how they were originally conceived as entities authorised on an occasional basis with a unique and exceptional role to play.



Decree 49 provided few guidelines on the criteria and procedure for the granting of permission. Perhaps some of the detail was set out in the "secret" provisions of article 3. Subsidiary enactments elaborated little further. Of particular importance was the November 1987 Instruction of the USSR Ministry of Finance on the registration procedure.<sup>434</sup> The Instruction provided that the USSR Ministry of Finance had the right to halt or refuse registration "in the instances where the documents submitted do not conform to USSR legislation on the creation and activities in the USSR of joint enterprises...". Once again the relevant Ministry was directed to ensure that before a joint enterprise was authorised to be created, its purposes had to be in the interests of the Soviet state.

The exceptional nature of the joint enterprise is best illustrated by the fact that by October 1987 only 12 joint enterprises had been registered, and by January 1988 this figure increased to only 23.<sup>435</sup> The joint enterprise was truly regarded as a concession, permitted to be created after much consideration within the Soviet polity and this no doubt was partly due to an acknowledgement that once a permission had been granted, the mechanisms available to the Soviet state to control their activities on an on-going basis were much more limited than in the case of the confirmation state enterprises.

Although the permitting process continued to ensure that the purpose of any joint enterprise was in the interests of the Soviet state, over time, the relevant authorising state entity became more devolved. Decree 1074 of September 1987 already provided that "Ministries and agencies of the USSR and Councils of Ministers of the union republics shall be granted the right to autonomously adopt decisions regarding questions of creation of joint enterprises with capitalist and developing countries".<sup>436</sup> This position was formally changed by an amendment to article 2 of Decree 49 by Decree 352 in March 1988 and then by Decree 385 in May 1989 which substituted the requirement for the consent of the Council of Ministers (ie government) of the USSR for the establishment of a joint enterprise for the consent of the relevant superior agency of administration.<sup>437</sup> As the *perestroika* reforms deepened, a less cautious approach was taken to registration and the presence of foreign capital in the Soviet economy; and by

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<sup>434</sup> O Poryadke Registratsii Sovmestnykh Predpriyatii, Mezhdunarodnykh Ob''edinenii i Organizatsii, Sovdavaemykh na Territorii SSSR s Uchastiem Sovetskikh i Inostrannykh Organizatsii Firm i Organov Upravleniya; supra n.397, p.386.

<sup>435</sup> Supra 397, p.5.

<sup>436</sup> O Dopolnitel'nykh Merakh po Sovershenstvovaniyu Vneshneekonomicheskoi Deyatel'nosti v Novykh Usloviyakh Khozyaistvovaniya, *Postanovleniya* (September 1987), no.1074, p.222, article 6. See also O Del'neishem Razvitii Vneshneekonomicheskoi Deyatel'nosti Gosudarstvennykh, Kooperativnykh i Inykh Obshchestvennykh Predpriyatii, Ob''edinenii i Organizatsii, *Postanovleniya* (December 1988), no. 1405, p.93.

<sup>437</sup> Supra n.407.



mid-1991 more than 3,000 joint enterprises were registered.<sup>438</sup> However, although more joint enterprises were permitted and although the authorising procedure as originally set out in Decree 49 had been substantially modified, the basic concept of the "concession" remained.

### 5.2.2 *Control over Activities - Constitutive Documents, Ultra Vires and Other Techniques*

The authorisation process ensured that the founders were required to detail clearly the purpose for the creation of the proposed joint enterprise in the TEO. This provided the state with the opportunity to evaluate the proposed purpose and to decide whether such a joint enterprise would be advantageous in light of the objective requirements of the Soviet economy.

Once authorised the state had to devise a mechanism to ensure that the joint enterprise's on-going activities continued to be based on the approved purposes. For reasons already outlined, this had to be achieved primarily through law and the state's role as sovereign, and was effected by requiring the constitutive documents of the joint enterprise to include a statement of the purposes of activity and then by relying on the Soviet law of *vires*.

Therefore, in addition to evaluating the TEO generally, the approval process included a consideration of the draft "constitutive documents". Decree 49 provided that the constitutive documents were "the contract creating the enterprise" (or constitutive contract) and "the charter".<sup>439</sup> There were few references to the constitutive contract in Decree 49 and it was not explicitly required by the legislation. However, in practice, most joint enterprises had a short form constitutive contract (in addition to a charter) setting out the basic commercial terms of the joint activity between the participants.<sup>440</sup> By contrast, Decree 49 provided that "a joint enterprise must have a charter...[which] shall determine" and set out the subject and purpose of the activities of the enterprise; its location; the composition of the participants; the amount of the charter fund; the amount of the participatory shares of the participants; the procedure for forming the charter fund (including in foreign currency); the structure, composition and competence of the organs of management of the enterprise; the procedure for the adoption of resolutions and the questions for which a unanimous decision is required; the procedure for liquidation of the enterprise; and other provisions not contrary to Soviet legislation and relating to the peculiarities of the joint enterprise.<sup>441</sup>

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<sup>438</sup> Supra n.399, p.11.

<sup>439</sup> Decree 49, article 8.

<sup>440</sup> For a history of the use of the constitutive contract in Soviet domestic associations before and after the joint enterprise legislation see N.V.Kozlova, *Uchreditel'nyi Dogovor o Sozdanii Kommercheskikh Obshchestv i Tovarishchestv* (Izdatel'stvo BEK:1994), pp.5-23.

<sup>441</sup> Decree 49, article 7.



Soviet legal textbooks elaborated on the kinds of provisions that should have been included in the charter; most of which were drawn from the charters of the former joint economic organisations established pursuant to international treaties with countries of SEV. A Model Constitutive Contract and Charter for a joint enterprise were examined and approved by the State Foreign-Economic Commission of the USSR Council of Ministers for use by ministries and agencies.<sup>442</sup> The importance of these Models lay far beyond their substantive provisions. Previously "model statutes" did exist for state enterprises,<sup>443</sup> however these were obligatory documents for use in connection with enterprises operating in specific sectors. By contrast, the joint enterprise Model Charter represented a move towards a state approved form of "precedent document" which was a starting point for negotiation. In this way, the joint enterprise legislation built on the existing legal permissive regime for the contract of joint activity<sup>444</sup> and began to erode the concept of mandatory state dictated enterprise law towards a more flexible contract based approach, setting out certain default rules.

Of particular importance in the charter was the purpose clause. It was derived from the TEO and would have been subject to careful scrutiny through the authorisation procedure. Its importance lay in the fact that it provided the linchpin for the future control or monitoring by the state over the activities of the joint enterprise by virtue of the operation of the general law on *vires*. Due to its status as a Soviet civil law juridical person, those articles of the civil codes relating to the *vires* of juridical persons in general also applied to joint enterprises.<sup>445</sup> The state as legal sovereign bolstered this general position by further providing in Decree 49 specifically that "a joint enterprise may be liquidated...if its activities do not correspond to the purposes and tasks provided in those [constitutive] documents".<sup>446</sup> As has been described, the question of *vires* was determined by reference to the specified purpose of activities rather than through an elaboration and listing of individual rights. The purpose could not have been stated to be "universal (unlimited)", and acts done contrary to the stated purposes could be deemed void.

While the state principally relied upon the *ultra vires* rule as a method for ringfencing the activities of the joint enterprise, it did retain, albeit in a reduced capacity, some of its "traditional Soviet" governance techniques. Three particular governance techniques were important. First, the state as owner of the Soviet participant had an indirect control over the

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<sup>442</sup> Supra n.397, pp.487-504.

<sup>443</sup> Supra n.273 and associated text.

<sup>444</sup> Supra n.336.

<sup>445</sup> Supra Section 3.4.1.

<sup>446</sup> Decree 49, article 51.



day-to-day activities of the joint enterprise to the extent that the Soviet participant was, or was required by legislation, to be involved in those operations.<sup>447</sup> Secondly, the state arguably retained the right of ownership over certain property of the joint enterprise. While the joint enterprise created a new subject of civil law, it was not intended to challenge the existing law on ownership and in particular the extent of state ownership of the means of production generally. As such, the use of state property would have been restricted by its "designation" prior to its allocation to the operative management of the Soviet participant and these restrictions should have continued to have applied upon the contribution of such property by the Soviet participant to the joint enterprise.<sup>448</sup> Indeed article 15 of Decree 49 hinted at the basic governance techniques of *vires* and property "designation" by providing that "the joint enterprise shall carry out in agreement with *Soviet legislation* the possession, use and disposal of its property in accordance with the *purposes of its activity* and *the designation of its property*" [emphasis added]. This statement in Decree 49 also illustrated a third technique - legal diktat.

### 5.2.3 *Mandatory Requirements and Economic Sovereignty*

As the joint enterprise was the first non-state owned industrial organisation introduced into the economy since the late 1920s, it had the capacity to undermine the state's existing economic sovereignty effected by way of state planning. Furthermore, it represented an anomaly in an economy that was otherwise wholly owned by the state. Clearly therefore the interaction between the joint enterprise and the wider Soviet economy, both in terms of theory and in terms of practice, was a critical issue for the founders. While the joint enterprise was to be exempt from mandatory planning instructions, as a matter of principle, Decree 49 was not intended to provide a bridgehead for the gradual erosion of state ownership of all of the means of production or of state control over the other actors within that economy. As a practical matter, state control over the wider economy did of course raise concerns for the founders, such as their ability to access raw materials within, and sell their production to, the domestic Soviet "market".<sup>449</sup>

In Decree 49 and other ancillary legislation, the Soviet state used its role as legal sovereign to impose mandatory legal requirements to ensure that it maintained its position as economic sovereign and had a continuing role in monitoring and controlling the activities of the joint

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<sup>447</sup> The rights of the Soviet participant as set out in Decree 49 are considered in more detail infra Section 5.2.4 below.

<sup>448</sup> The property regime of joint enterprises is considered in more detail infra Section 5.4.2.

<sup>449</sup> See infra Section 5.3.2.



enterprise. Decree 49 did not however explicitly acknowledge the need to regulate the detail of the relationship between the joint enterprise and the wider Soviet economy nor the fact that it was intended that the state monopoly in all branches of the industrial economy would be maintained notwithstanding the presence of non-state owned joint enterprises. It is probable that this lack of express acknowledgement in the legislation was due to the fact that the joint enterprise was introduced and characterised as a feature of foreign relations law, and extensive provisions relating to its relationship within the domestic economy would have made it more difficult for legislators to have finessed its "real" significance as a domestic Soviet juridical person and as an exception to the general rule of state ownership of the means of production. Furthermore, it is unlikely that in 1987 the Soviet polity was sure of exactly how the joint enterprise was intended to operate as a general matter within an otherwise command economy.

Although there was no express regulation of the relationship between the joint enterprise and the wider Soviet economy in a specific section of the decree, Decree 49 did contain a number of relevant provisions that were scattered throughout the enactment that addressed the question of the preservation of the state's monopolies generally and the state's ability to monitor and thereby control any activities of the joint enterprises.<sup>450</sup>

Preservation of the state monopoly of banking operations and general monitoring and control over the assets and responsibilities of joint enterprises was ensured by the terms of articles 27-29 of Decree 49. These provisions required cash assets of a joint enterprise to be deposited in a ruble or currency account with the State Bank of the USSR or the Foreign Trade Bank of the USSR, and then gave the state the right to have direct access to information relating to the accounts of the joint enterprise and the right to effect control over its use and repayment of loans.

Article 45 went on to require that the joint enterprise keep operational, bookkeeping and statistical records in the procedure prevailing in the USSR for Soviet state enterprises and that "the forms for such records and reports shall be confirmed by the USSR Ministry of Finance jointly with the Central Statistical Administration of the USSR." The article then explicitly noted that breach of these bookkeeping and filing requirements would lead to "responsibility in accordance with Soviet legislation." Further monitoring was provided for by article 38 which stated that financial agencies shall have the right to verify the correctness of the calculation of tax by joint enterprises.

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These are also further considered infra Section 5.3.2.



In terms of general operations and its nexus with the state plan and ancillary monopolies, Decree 49 reminded the participants in various different places of the need to obtain the relevant consents: imports and exports could only be carried out "on the basis of authorisations issued in the procedure established by legislation of the USSR";<sup>451</sup> the building of plants and installations "shall be subject to consent in the procedure established by the State Construction Committee of the USSR";<sup>452</sup> and "carriage of goods of joint enterprises shall be effectuated in the procedure established for Soviet organisations".<sup>453</sup> Perhaps the most telling provision of Decree 49 in relation to the operations of the joint enterprise was not a restrictive, but a permissive article: article 24 provided that "a joint enterprise shall have the right to carry on correspondence, telegraph, teletype and telephone communications with organisations of other countries." The regime of state control over the economy was so tight that it was considered necessary to provide explicitly for something that would seem to any foreign investor as a basic and almost "assumed" right - the right to communicate with the wider international market. However, the Soviet state was still concerned about information on the domestic economy being made available other than through official state channels; and as such, article 45 provided as an exception to this right to communicate that "joint enterprises may not distribute any reports or information to states and other agencies of foreign states".

While securing the state monopoly over banking activities, access to information and ensuring general compliance with prevailing authorisation requirements, the mandatory rules for the operations of the joint enterprise also initially included the requirement to take out "compulsory insurance at the insurances agencies of the USSR";<sup>454</sup> the requirement that the sale of products shall be in the Soviet market and "effected by payment in roubles through the corresponding Soviet foreign trade organisations at contractual prices taking into account prices on the world market";<sup>455</sup> and the requirement that "the personnel of joint enterprises shall be made up principally of Soviet citizens".<sup>456</sup> Decree 49 elaborated, noting that joint enterprises were obliged to conclude "collective contracts with the trade union organisation at the enterprise" and that general labour protection legislation applied in addition to the

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<sup>451</sup> Decree 49, article 24.

<sup>452</sup> Decree 49, article 34.

<sup>453</sup> Decree 49, article 35.

<sup>454</sup> Decree 49, article 14. Although this article was amended by Decree 385 to provide that the risks of joint enterprises "shall be insured by agreement of the parties".

<sup>455</sup> Decree 49, article 26. Although this was amended by Decree 352 to provide that such realisation "shall be determined by the joint enterprise by agreement with Soviet enterprises and organisations".

<sup>456</sup> Decree 49, article 47.



requirements to make deductions to the USSR State Budget for social insurance and pension contributions of the workforce.<sup>457</sup>

Although seemingly randomly placed throughout the decree and rudimentary in their scope, all of the above mentioned provisions should be regarded as addressing the fundamental issue of the preservation of the role of the state as economic sovereign and the right of the state to monitor activities of the joint enterprise. Their brevity and place within Decree 49 only attests to the fact that this relationship was not entirely developed at the time of drafting the legislation and evidenced the need to finesse the real significance of the joint enterprise. However what is consistently apparent from all these provisions is that there was no intention in 1987 of the joint enterprise becoming the first step to a two tier economy, one controlled by the state and one that was not.

#### 5.2.4 *Indirect Control - The Exclusive Rights of the Soviet Participant*

While the contract-based concession model gives rise to a state governance regime based on its retreat from its place as sole and direct owner of the enterprise, one of the participants of the joint enterprise was of course always Soviet and invariably this participant was state-owned. As such, in addition to its role as sovereign, the state had the opportunity in part to maintain its influence over the activities of a joint enterprise through its ownership of the Soviet participant.

This additional role of the state and its place in the governance regime of the contract-based concession enterprise was developed through the granting of various "exclusive" rights of the Soviet party. Within the contract-based concession model, this governance technique, which used legislative rights to favour one participant over another, was broadly anachronistic because the relationship between the participants was intended to be "on the basis of contracts". And as *perestroika* deepened, these "exclusive" rights were gradually removed.

Decree 49 provided that participants had to be "juridical persons" in their own right, and on the Soviet side these were invariably state-owned.<sup>458</sup> The Soviet participant was given control over the application process,<sup>459</sup> and its subsequent position within the enterprise was entrenched by the requirement that the Soviet participant had to have at least a 51% participatory share in the charter fund.<sup>460</sup> Decree 49 also required the chairman *and* the

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<sup>457</sup> Decree 49, Part VI.

<sup>458</sup> Decree 49, articles 1 and 4.

<sup>459</sup> Decree 49, article 2, paragraph 1.

<sup>460</sup> Decree 49, article 5. See also *infra* Section 5.4.2.



director general to be Soviet citizens.<sup>461</sup> The participatory share of the Soviet participant in the enterprise was protected by restrictions on transfer of participatory shares and pre-emption rights,<sup>462</sup> and article 16 provided that, following agreement between the participants, a transfer of a participatory share in the joint enterprise "in each separate instance shall take place [only] with the authorisation of the State Foreign-Economic Commission of the Council of Ministers of the USSR [ie the government]."

However, in almost every instance where the original version of Decree 49 provided more favourable treatment for the Soviet participant, amendments were subsequently made to redress the balance.<sup>463</sup> Decree 385 removed the 51% requirement, providing that participatory shares in the charter fund would be "determined by arrangement between them [the participants]" and also provided that a foreign citizen could take the post of either the chairman or the director general. The involvement of a commission of the USSR government in relation to each participatory share transfer, as in the case of the government's involvement in the authorisation procedure itself, was soon recognised as impractical, and Decree 352 gave the right to authorise participatory share transfers to ministries and agencies of the USSR, or the governments of the various union republics which had adopted the resolution on the creation of the relevant joint enterprise. Finally, the transfer provisions were amended yet again by Decree 385 in May 1989 which removed completely the requirement for authorisation of transfers.

### 5.3 Inducement - The Nature of the Concession

While the Soviet state weaved a new control regime based upon authorisations, legal imperatives and its role as sovereign, it also had to provide the necessary conditions and incentives for attracting foreign investors to participate within the economy in the manner envisaged. This was primarily achieved by creating the opportunity for "doing business" within the domestic Soviet economy on the basis of an association that was recognised as a juridical person, free from compulsory state planning instructions, with limited responsibility.

#### 5.3.1 *Juridical Personality*

Joint ventures, even with capitalist countries, were not unknown within the socialist legal systems of the 1970s and 1980s. During that time there were a variety of approaches taken, including the setting up of joint ventures which operated wholly outside the internal planned

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<sup>461</sup> Decree 49, article 21.

<sup>462</sup> Decree 49, article 16. The foreign participant was not given a corresponding pre-emption right.

<sup>463</sup> For references to amending decrees, see *supra* n.407.



system, such as in Rumania, and those that were more integrated, such as in Yugoslavia.<sup>464</sup> Decree 49 took the radical approach of providing explicitly that joint enterprises "shall be juridical persons according to Soviet legislation" and shall "acquire the rights of a juridical person from the moment of registration" with the USSR Ministry of Finance.<sup>465</sup> This both brought the joint enterprise firmly within the mainstream of Soviet domestic civil law and at the same time distinguished the joint enterprise from its roots in the contract for joint activity that was not a juridical person. It was the characteristic of juridical personality that was the key element of the concession: it was the first time since the 1920s that juridical personality had been conferred by Soviet law upon an association operating within the industrial economy that was not wholly owned by the state. There were no provisions of the 1961 FPCivL that contemplated its creation and thus its status fell within the residual category of the list in Article 11 of the 1961 FPCivL.<sup>466</sup> Braginskii noted of joint enterprises "firstly they are deemed to be juridical persons in the USSR in accordance with prevailing legislation in our country, secondly they are domestic legal persons [as opposed to international legal entities] and thirdly...they must be guided by prevailing norms in the USSR unless inter-state or inter-governmental agreements provide otherwise."<sup>467</sup> As a juridical person, the joint enterprise was deemed to have organisational unity (ie a charter (in addition to a constitutive contract)); solitary property;<sup>468</sup> autonomous property responsibility;<sup>469</sup> and the right to act on its own behalf in economic turnover and bear consequential responsibilities.<sup>470</sup> General norms relating to its operation and details of the authorisation process were set out in specific provisions of Decree 49 itself.<sup>471</sup>

While the joint enterprise was a juridical person that operated within the framework of Soviet civil law, it was a rather "special" juridical person in two ways: first, although it was subject to the general and mandatory rules of civil law, it operated on the principle of "full *khozraschet*, non-subsidy and self-financing", carrying on its activities outside the system of

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<sup>464</sup> On different types of joint ventures within the socialist legal systems and outside, see N. N. Voznersenskaya, *Pravovye Formy Sovmestnogo Predprinimatel'stva i Praktika SSSR*, *SGiP* (1985), no.3, p.59.

<sup>465</sup> Decree 49, articles 6 and 9.

<sup>466</sup> *Supra* n.410.

<sup>467</sup> *Supra* n.397, p.89.

<sup>468</sup> The nature of this "solitary property" is considered in more detail below in Section 5.4.2.2.

<sup>469</sup> The nature of this "autonomous property responsibility" is considered in more detail *infra* Section 5.3.2.

<sup>470</sup> On the juridical personality generally, see *supra* Section 3.3.

<sup>471</sup> *Supra* Section 5.2.3.



compulsory state planning instructions; and secondly, Decree 49, and additionally the charter, provided for "special privileges" in particular relating to tax.

### 5.3.2 *Full Khozraschet, Non-Subsidy and Self-financing - Responsibility and Insolvency*

Decree 49 provided that joint enterprises "shall operate on the basis of full *khozraschet*, non-subsidy and self-financing".<sup>472</sup> While the concept of *khozraschet* had been in existence since the 1920s and had developed into "internal" and other types of *khozraschet*,<sup>473</sup> and while the development of "genuine *khozraschet* and self-financing" specifically had been a feature of recent reforms in the industrial economy,<sup>474</sup> the formulation of "full *khozraschet*, non-subsidy and self-financing" was entirely new in the area of foreign trade law. Although there was no express definition, in the context of the joint enterprise, this formulation was probably intended to highlight the joint enterprise's exceptional character as operating outside the command economy and the system of state subsidies. It set out the cornerstones for the basis of operations: a joint enterprise had to have sufficient assets necessary for its activities, and those activities were to be carried out free from the constraints of state orders based in the context of a responsibility regime more akin to "real" limited liability.<sup>475</sup>

Article 23 of Decree 49 explicitly stated the general principle that "a joint enterprise shall independently work out and confirm the program of its economic activities. State agencies of the USSR shall not establish binding planning tasks for a joint enterprise and the sale of its products shall not be guaranteed". It was therefore intended that the joint enterprise would operate on the basis of the general rules of civil law and within the domestic economy but outside the planning system. Unfortunately, as has been noted, Decree 49 did not include any coherent attempt to set out the way in which these "autonomous" juridical persons would carry out operations in an otherwise command economy. In the same manner that Decree 49 had included in an *ad hoc* way references that placed the joint enterprise within the constraints of the wider Soviet command economy,<sup>476</sup> Decree 49 and subordinate legislation also contained, in a somewhat random fashion, a number of provisions aimed at facilitating the operations of joint enterprises within that economy. For example, the "Procedure for the Material-Technical Supply of Joint Enterprises, Created on the Territory of the USSR with Participation of Other Countries and Foreign Firms and Sale of their Products" was adopted to

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<sup>472</sup> Decree 49, article 6.

<sup>473</sup> See *supra* Section 2.2.

<sup>474</sup> For a summary of the development of the "new economic conditions" and the introduction of the concept of "full *khozraschet* and self-financing" during mid 1985 and 1986, see *infra* Section 6.3.2.

<sup>475</sup> Cf the regime of autonomous property responsibility in the confirmation model *supra* Section 3.3.

<sup>476</sup> *Supra* Section 5.2.3.



provide a framework for the sale to joint enterprises of supplies through contracts with state agencies.<sup>477</sup> As *perestroika* advanced and state enterprises were given more control over their operations following the 1987 State Enterprise Law,<sup>478</sup> joint enterprises became increasingly able to source goods directly from state enterprises on the basis of the civil law of contract. Furthermore, in order to facilitate the operations of joint enterprises within the Soviet economy but outside the plan, a number of legislative enactments were adopted, aimed at ensuring that arrangements of some kind were in place to regulate the areas of import-export activities, currency regulation, prices and banking, in addition to the supply of goods.<sup>479</sup>

Economic autonomy of joint enterprises was evidenced by the first steps in the legislation on industrial organisations of the *perestroika* period away from a regime of autonomous property responsibility towards a regime of "real" limited liability. Decree 49 set out two rules relating to their responsibility: first, the joint enterprise shall be "responsible for its obligations with *all* the property which belongs to it" [emphasis added]; and secondly, the state and participants shall not be responsible for the liabilities of the joint enterprise and vice versa.<sup>480</sup>

"Autonomous property responsibility" understood within the framework of the confirmation model did not have its functional genesis from within the insolvency context - indeed few state enterprises were liquidated - most were reorganised.<sup>481</sup> By contrast, full *khozraschet*, non-subsidy and self-financing indicated a move towards a rule of "real" limited liability understood by reference to the insolvency situation: the joint enterprise should not rely on the state to act as a *de facto* "guarantor" of its operations;<sup>482</sup> *all* the assets of the joint enterprise were to be available to creditors;<sup>483</sup> and its responsibilities were to be separated from those of

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<sup>477</sup> Poryadok Material'no-tekhnicheskogo Snabzheniya Sovmestnykh Predpriyatii, Sozdavaemykh na Territorii SSSR s Uchastiem Drugikh Stran i Zarubezhnykh Firm, i Sbyta ikh Produktsii, *Vneshnaya Torgovla* (1988) no.1, p.45. Due to presence of the joint enterprise as outside the planned economy, one commentator noted "in economic life however, it is evident that the joint enterprise is not able to function as a normal subject of economic activities", see *supra* n.409, p.50.

<sup>478</sup> *Infra* Section 6.3.

<sup>479</sup> On the problematic nature of the regime of supply of goods to and from joint enterprises generally, see *supra* n.409, pp.47-60.

<sup>480</sup> Decree 49, article 18.

<sup>481</sup> *Supra* Section 3.3.

<sup>482</sup> In relation to state enterprises operating within the planned economy, the state, while separated as a matter of law from the responsibility of the enterprise, in practice supported its activities where the existence of the enterprise was deemed necessary (*supra* n.269).

<sup>483</sup> The availability of "all" assets was a significant departure from the autonomous property responsibility regime of the confirmation enterprise where most fixed assets of state enterprise were excluded from the pool of funds to which creditors could seek recovery for outstanding debts (see, *supra* n.270). However, the status of the joint enterprise's property and its availability in the context of a liquidation needs also to be understood within the context of its ownership regime. In particular, the concept of "all" assets may



its participants. The independent property status of the joint enterprise was further ensured by article 15 of Decree 49 which provided that "its property shall not be subject to requisition or confiscation in an administrative proceeding".

With a shift towards the notion of non-subsidy and self-financing, the insolvency situation became a more distinct possibility in practice. Although the state no longer owned the joint enterprise directly or outright, it was clearly "interested" in ensuring the continued successful operation of the joint enterprises in general. However the exclusion of the roles of the state as creator-owner, and arguably as property-owner, made it more difficult for the state to control the activities of the joint enterprise; and furthermore, the move to full *khozraschet*, non-subsidy and self-financing made its operations increasingly vulnerable to market forces. The state therefore by legislative diktat in Decree 49 (adopting its role as legislative sovereign) attempted to reduce the insolvency risk through the requirement of a reserve fund, and the allocation of any residual risk first to the foreign participant.

Soviet law conceived of charter capital as protection for creditors and hence as protection against insolvency.<sup>484</sup> On this basis, in addition to the charter fund, Decree 49 required the setting up of "a reserve fund and other funds needed for the activities thereof and for the social development of the [labour] collective."<sup>485</sup> Deductions to the reserve fund were required to be made until it reached 25% of the charter fund. The concept of a reserve fund was novel to the extent that it did not appear in either the Enterprise Statute or the Production Association Statute. It was regarded as a fund for additional protection against downturns in the economy that could be debited to meet the demands of creditors if necessary so as to mitigate against the risk of insolvency. There were also other mandatory provisions of Decree 49 that seemed to be aimed at protecting the joint enterprise from insolvency under this new regime of full *khozraschet*, non-subsidy and self-financing. For example, article 25 required that "all currency expenditures of a joint enterprise...must be ensured by the joint enterprise from receipts from the realisation of its products...". This statement can be viewed as a

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have been severely limited if the joint enterprise did not have the right of ownership (see *infra* Section 5.4.2).

<sup>484</sup> This is a view which, as Butler commented, "has long been overtaken in the West by more sophisticated structures" (W.E.Butler, *Russian Law* (Oxford University Press:1999), p.427). Black, Kraakman and Tarassova noted that "charter capital has two central weaknesses as a device for protecting investors in a joint stock company: (i) it establishes a floor on the company's shareholder capital (the amount of the company's net assets) that may have little relationship to a company's actual shareholder capital; and (ii) it establishes this floor based on the book value of a company's assets, which may be very different from the assets' real value" (Bernard S. Black, Reinier Kraakman, Anna S. Tarassova, *Guide to the Russian Law on Joint Stock Companies* (Kluwer Law International:1998), pp.207-208).

<sup>485</sup> Decree 49, article 30. On participatory shares in the charter fund, see *infra* n.506.



declaration of what it means to operate on the basis of full *khozraschet*, but may also have been included as a direction to act in what the Soviet state considered to be an economically prudent manner,<sup>486</sup> in much the same way as the state in the Enterprise Statute had directed its state enterprises to "ensure high quality...of products".<sup>487</sup>

In addition to requiring by diktat that participants make provision for downturns in the business cycle, the state also "adjusted" the insolvency waterfall, to allocate insolvency risk first upon the foreign participant. Upon a liquidation of the joint enterprise, article 52 of Decree 49 provided that the "foreign participant...shall receive the right to the return of his contribution in cash or in the form of goods in accordance with the *remaining value* of the contribution at the moment of liquidation of the enterprise *after payment of his obligations to Soviet participants and third persons*" [emphasis added]. The position of the foreign participant was therefore compromised: first by suggesting that contributions may be subject to some form of reduction or amortisation (hence the reference to "the remaining value"); and secondly, by placing the foreign participant in a "super-subordinated" position, with a right to be paid a liquidation dividend only after obligations to the Soviet participant had been satisfied.

### 5.3.3 *Charter Privileges*

In addition to the right of juridical personality and limited liability, the concession of the joint enterprise provided a number of privileges, principally in the area of taxation. These were as a matter of practice generally reflected in the drafting of the charters. A basic rate of 30% of tax on profit after deductions was levied; however Decree 49 provided that a joint enterprise was exempt from paying this tax "for the first two years of its activity" and further gave the USSR Ministry of Finance the right to decrease the amount of tax, or completely exempt specific tax payers from tax.<sup>488</sup> To incentivise the creation of joint enterprises still further, Decree 352 of 1988 increased the duration of the tax holiday by providing that the two year period commenced at a later date - "from the moment of receiving a declared profit". This addressed the concern that joint enterprises may not have made any profits during their first

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<sup>486</sup> Article 25 can also be more radically interpreted as limiting the availability of debt financing, requiring that all expenditure be financed solely out of cash flow.

<sup>487</sup> Supra Section 3.4.3 which develops this idea of coercive law.

<sup>488</sup> Decree 49, article 36. The concept of tax privileges was also established in the implementing Edict of 13 January 1987 and the amendments thereto.



two start-up years. Other privileges and guarantees included the right to transfer abroad foreign currency distributions of profits.<sup>489</sup>

The approval of the charter by the USSR government during the authorisation procedure<sup>490</sup> raised the question as to whether the charter had a quasi-legislative status. The characterisation of the charter as a quasi-legislative document was not without precedent (for example, pre-revolutionary Russian charters,<sup>491</sup> and the NEP era legislation on concessions were deemed to have quasi-legislative status<sup>492</sup>). This quasi-legislative status of the charter opened up the possibility for providing for special privileges in the charter that sought to supplement, and in some instances even vary, prevailing legislation itself.

The status of the constitutive documents of the joint enterprise was always a matter of Soviet "doctrine" which itself varied over time. The interpretation of their status as a "quasi-legislative act" was generally accepted during the first few years after 1987 when participants often attempted to include in the provisions of their charters, privileges and guarantees or "clarifications" of existing legislation (such as a statement giving the joint enterprise the right of ownership).<sup>493</sup> Doctrine then changed, partly as a result of the numbers of joint enterprises being registered, partly as a result of the streamlined registration procedure for joint enterprises which removed the need for USSR Council of Ministers approval, and partly as a result of the introduction of other forms of foreign investment vehicles. Gradually therefore the ambiguity of the status of the charter became resolved and further privileges became increasingly rare as state agencies demanded compliance with prevailing legislation notwithstanding any provisions to the contrary as set out in charters that had been registered.

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<sup>489</sup> Decree 49, article 32.

<sup>490</sup> Supra Section 5.2.1.

<sup>491</sup> Charters of the pre-revolutionary corporations of nineteenth century Russia frequently provided for all sorts of opt-outs from prevailing norms. Owen noted that "the irony was that, in one sense the [Corporate] law of 1836 was totally unnecessary, Every corporate charter bore the emperor's signature and thus it was regarded by most jurists as having "the force of law". (supra n.429).

<sup>492</sup> The 1920 Dekret on Concessions contained a grandfather clause guaranteeing that changes in legislation would not effect the operation of charters that had been approved (supra n.386). The Main Concessionary Committee attached to the USSR Council of People's Commissars had the right: to review draft charters including those provisions which provided for exemptions from existing legislation; and to submit them for approval by the USSR Council of People's Commissars (the then USSR Government) (*Ob Ychrezhdenii Glavnogo Kontsessionnogo Komiteta pri Soveta Narodnykh Komissarov Soyuza Sovetskikh Sotsialisticheskikh Respublik, SU* (1923), no.96, item 952). The decree implementing the 1927 Statute on Joint-Stock Societies specifically provided in article 11 that in the event that the provisions of charters of concession joint-stock societies contradicted the provisions of the 1927 Statute, the former would prevail notwithstanding the general rule set out in article 6 that all joint-stock societies had to amend their charters to ensure compliance with the 1927 Statute or they would be void.

<sup>493</sup> On the right of ownership see infra Section 5.4.2.



#### 5.3.4 *Dispute Resolution*

The contract-based concession model contemplated within the organisational forum the presence of interests other than the Soviet state. The logic of this model therefore opened up the possibility not only for conflicts between participants but also between a participant (or the joint enterprise) and the state itself. Any procedure for the resolution of disputes against the state would have directly compromised the principle of socialist legality and the place of the Soviet state as the source, and not the subject, of "legality".<sup>494</sup>

Despite the clear possibility of its occurrence, Decree 49 stepped back from openly contemplating a procedure for dispute resolution where the state was a litigant. Article 20 provided that "disputes of joint enterprises with Soviet state, cooperative and other social organisations, and disputes between each other and also between participants" shall be decided "in accordance with legislation of the USSR and shall be considered in the courts of the USSR or by arrangement of the parties in an arbitration tribunal." This envisaged litigation between juridical persons and participants *inter se* (and even between juridical persons owned by the state) but not with the state itself. It took several more years before the Soviet state would explicitly acknowledge the move away from socialist legality to the principle of the rule of law state, and the right of action against the state itself. However before the erosion of the principle of socialist legality, culminating in the 1990 new economic constitution, the joint enterprise was the first organisational forum that posed questions as to the coherence and applicability of the doctrine of socialist legality in an economy where the state no longer owned all the means of production.

#### 5.4 **Governance - The Regulation and Protection of the Interests of the Participants**

The governance regime of the contract-based concession enterprise sought to provide a framework for the balancing of the interests of the various participants *inter se*. Traditionally a governance regime of a body corporate, and the rights and obligations associated with it, often just reflect the characteristics of the particular ownership interest issued by the applicable juridical person.<sup>495</sup> Soviet law did not however contain a developed notion of the ownership interest; and instead these were structured relationships by reference to the quasi-feudal concept of forms of ownership. As has been argued, this law on ownership was particularly unsuitable for the legal regulation of property rights between an owner and a juridical person in a regime of fragmented ownership based on the need to attract equity

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<sup>494</sup> On socialist legality, see *supra* Section 2.2.

<sup>495</sup> See *supra* Section 2.5.



capital. And the joint enterprise was perhaps the first example of such a juridical person since the 1920s.

#### 5.4.1 *Negotiating the Constitutive Contracts*

In addition to providing the legal basis for the authorisation procedure, the constitutive contract and charter more generally set out the basic terms for the co-operation between the participants and the nature of their interests.<sup>496</sup>

Soviet legal theory as a matter of principle divided norms into "imperative" and "supplementary"; and only the latter were able to be varied by contract. In the context of joint enterprises, Professor Braginskii noted that "the norms of Decrees 48 and 49 on the rights and obligations of the participants of joint economic organisations have an imperative character and the waiver of them in the constitutive documents is prohibited."<sup>497</sup> However, despite the existence of these imperatives, in common with the law relating to the contract for joint activity, Decree 49 contained relatively few provisions setting out the rights and obligations of the participants. Within the context of agreeing the constitutive documents, this therefore left much room for negotiating the exact nature of the relationship between participants.<sup>498</sup> As has been noted, subsequent amendments to Decree 49 reduced still further the number of these mandatory provisions and this just increased the possibility for "contracting".<sup>499</sup> The only general limitation in practice on the scope for negotiations may have been set by the Model Charter,<sup>500</sup> for the greater the departure from the form of the Model Charter, the more difficult it may have been to register the charter with the appropriate agency.

Decree 49 in fact explicitly recognised the joint enterprise as an organisation "created...on the basis of contracts concluded with the participants".<sup>501</sup> This was of enormous significance for the history of the Soviet of industrial organisation. It was the first time since the 1922 RSFSR Civil Code that the contractual basis for a domestic juridical person was recognised. While in 1987 there was no intention of redeveloping the basic principles of juridical personality, the

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<sup>496</sup> Decree 49, article 7.

<sup>497</sup> Supra n.397, p.66.

<sup>498</sup> As noted by N.N.Voznesenskaya "at the present time, concrete legal regulation of joint enterprises is extremely incomplete and many important questions, which as a rule are regulated by law in other countries, are still in our [legal system] regulated by agreement [between the parties]" (N.N.Voznesenskaya, *Pravovoe Status Sovmestnykh Predpriyatii, Sozdavaemykh na Territorii SSSR s Uchastiem Firm Kapitalisticheskikh Stran*, p.27).

<sup>499</sup> Supra Section 5.2.4.

<sup>500</sup> See supra Section 5.2.2.

<sup>501</sup> Decree 49, article 1.



adoption of Decree 49 and the granting of juridical personality to a contract based association posed a fundamental challenge to the very heart of Soviet civil law theory and the law on ownership which, in particular, was inadequate to regulate coherently legal relations based on contract, with fragmented interests present within the organisational forum.

#### 5.4.2 *Ownership Interests and the Joint Enterprise*

Article 11 of the 1961 FPCivilL listed *specific* Soviet juridical persons and implicitly categorised them by reference to the civil law forms of ownership.<sup>502</sup> As already noted, there was in addition to this specific list, a "catch-all" category in article 11 providing for the right of juridical status of "other organisations" deemed to be juridical persons in accordance with specific pieces of USSR legislation. And the joint enterprise fell into this catch-all category. Unfortunately there was no attendant form of ownership that was linked to this catch-all category and as such, at the level of primary civil law legislation, the ownership regime of the joint enterprise was always uncertain. This left open two distinct questions: did the participants "own" the joint enterprise? and did the joint enterprise have the right of ownership?

##### 5.4.2.1 *Ownership of the Joint Enterprise*

From the previous analysis presented in this study,<sup>503</sup> it should come as no surprise that, from the perspective of developing an ownership framework for a juridical person with multiple owners and foreign investment, Decree 49 was hopelessly inadequate. Most importantly, while giving the joint enterprise juridical personality, Decree 49 did not explicitly provide for the concept of an ownership interest issued by the joint enterprise to the participants that could have provided the rationale for elaborating a set of rights and obligations that clearly established the legal basis of the relationship between the participants and the joint enterprise itself; and furthermore would have constituted a move towards the concept of equity capital.

Unfortunately, not only did Decree 49 fail to provide explicitly for the existence of an ownership interest of a joint enterprise but, like the 1922 simple partnership,<sup>504</sup> it also adopted a plethora of inconsistent terminology that seemed to touch upon this central point without

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<sup>502</sup> Supra Section 2.5.

<sup>503</sup> See supra Section 2.3 on the nature of the Soviet law on ownership, Section 2.5 on the absence of the concept of the ownership interest and its importance for a body corporate with fragmented ownership, and Sections 2.4.2 and 4.6 on the uncertain regimes relating to the ownership of collective farms and associations formed on the basis for the contract for joint activity. The argument is developed more fully in Chapter 7.

<sup>504</sup> Supra Section 4.1.



resolving it. In particular it contemplated a "contribution" ("*vkklad*");<sup>505</sup> a "participatory share" ("*dolya*");<sup>506</sup> and a "participatory share participation" ("*dolevomu uchastiyu*").<sup>507</sup> Most importantly, in relation to the sale of the interest of a participant in a joint enterprise, Decree 49 provided for the right to transfer their participatory share in the joint enterprise ("*dolya v sovmestnom predpriyatii*") as well as for the preferential right of Soviet citizens to acquire the participatory shares ("*dolei*") of the foreign participants.<sup>508</sup>

Collective farm legislation used the term "share" ("*pai*") to describe the interest of collective farmers in the share fund, and the argument that references to "a share" in the context of collective farm law were to an ownership interest of the collective farm has already been analysed.<sup>509</sup> Decree 49 by contrast used the terminology of "contributions" and "participatory shares" ("*dolya*") (and not of "shares"). Once again, albeit with different terminology, it is tempting to consider the participatory share as evidence of an equity ownership interest, however, for different reasons, once again, this was unlikely.

As discussed, as a general matter, the concept of an ownership interest of a juridical person was functionally redundant within the mainstream Soviet legal and economic system. More specifically, in the context of the joint enterprise, the presence of ownership interests characterised as tradable equity participations would have undermined the rationale for the joint enterprise as a concession granted to particular investors with particular skills, a particular approach and a particular business plan that the Soviet authorities were prepared to authorise.

Under the quasi-feudal Soviet law on ownership, the state retained ownership of all the means of production. In the industrial economy this was preserved through the concept of industrial juridical persons without the right of ownership, allocated property by way of operative management.<sup>510</sup> Applying this paradigm to the "new" juridical person within the industrial economy, the joint enterprise, it should be assumed that property "contributed" to the joint

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<sup>505</sup> Decree 49, article 10 (which contemplated a charter fund "formed at the expense of contributions of the participants" which could be increased from "profits" and "additional contributions") and Decree 49, article 12 (contribution to the charter fund).

<sup>506</sup> Decree 49, article 5 (which contemplated a specific participatory share: a "participatory share in the charter fund") and Decree 49, article 7 (which did not, referring only to "the amount of the participatory share of the participants" (without stating to what this share related)).

<sup>507</sup> Decree 49, article 31 (which provided that profits were to be divided proportionally to each participant's participatory share participation ("*dolevomu uchastiyu*") in the charter fund).

<sup>508</sup> Decree 49, article 16.

<sup>509</sup> Supra Section 2.4.2.

<sup>510</sup> Supra Sections 2.3.1 and 3.4.2.



enterprise by the participants was not offered up in exchange for an ownership interest (ie equity), but rather contributed by way of allocation for use, possession and disposition while ownership was retained by the participants.

Not only did general Soviet legal theory support this view of the "participatory share", not as an ownership interest, but as a direct right to the property allocated to the joint enterprise, but also, in contrast to the concept of the "share" used in collective farm law, the language of the "participatory share" and "contributions" incorporated directly the terminology of common ownership and the contract for joint activity. As discussed, common ownership was a mechanism for the pooling of resources by different owners where ownership was retained in the common fund, either on a joint or participatory share basis.<sup>511</sup> This analysis is further supported by the ownership regime of the joint economic organisations established under the 1983 edict. It was specifically provided that contributed property remained in "common socialist ownership" by way of "operative management".<sup>512</sup>

This interpretation of participants to the joint enterprise as bereft of ownership interests, but as continuing owners of contributed property, is consistent with the analysis presented in this study of ownership relations in the context of collective farms, the contract for joint activity and the relationship between the state and state enterprises. Furthermore, the general theory of Soviet ownership law and the concession approach is consistent with this view. This "look through" of ownership rights would obviously be reinforced by a conclusion that the joint enterprise, like the state enterprise, did not ever have the right of ownership and never constituted one of the exceptions to the principle of state ownership of all of the means of production.

#### 5.4.2.2 *Ownership by the Joint Enterprise*

The joint enterprise was a juridical person with the right to possession, use and disposition of property.<sup>513</sup> It had a separate balance sheet, and as such Decree 49 explicitly referred to "property of joint enterprises"<sup>514</sup> and "its property".<sup>515</sup> More generally, Decree 49 provided for "property rights of a joint enterprise",<sup>516</sup> and the transfer of "industrial property rights to a

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<sup>511</sup> Supra Sections 2.6 and 4.6.

<sup>512</sup> Supra n.400.

<sup>513</sup> Decree 49, article 15.

<sup>514</sup> Ibid.

<sup>515</sup> Decree 49, article 44.

<sup>516</sup> Decree 49, article 15.



joint enterprise",<sup>517</sup> and characterised property as "belonging to" ("*prinadlezhashchim emu*") the joint enterprise.

This drafting may have suggested that the joint enterprise had the right of ownership. However, by analysing this framework within the existing terminology of Soviet law, it is more probable that the joint enterprise was to be treated like the state enterprise - ie as an industrial organisation without the right of ownership to which property was allocated by way of operative management. In fact the drafting in Decree 49 which set out the property rights of the joint enterprise was entirely consistent with the regime of operative management as applied to state enterprises.<sup>518</sup>

The regime of operative management within the context of the state enterprise also contemplated the right of possession, use, and disposition of property. However, while such rights in the case of ownership were limited only by general principles of Soviet civil law, in the case of operative management, they were also limited by restrictions placed by the owner through the concept of "designation". The characteristic of a separate balance sheet, and hence the references to property "of" a state enterprise, was also a feature of the operative management framework. The genitive case entailed only allocation and not necessarily ownership. Finally, the potential to acquire rights was not inconsistent with the absence of the right of ownership, as Soviet law distinguished rights (that could be acquired by any person) from property (which could only be owned by persons with the right of ownership).<sup>519</sup>

References to "designation" of the property of a joint enterprise,<sup>520</sup> and the absence of a clear statement that the joint enterprise had the right of ownership leads to the relatively certain conclusion that joint enterprises did not have the right of ownership. If Decree 49 was to create a new form of ownership for the joint enterprise, and hence create such a fundamental change or challenge to the existing civil law framework, it is unlikely that this would have sought to have been achieved through a decree (rather than a law) without explicit drafting on the point and through an enactment that strictly fell within the law of foreign relations (and not civil law). However, unfortunately, while Decree 49 used terminology and understandings drawn from the existing operative management regime, it did not explicitly provide for its application and hence some doubt remained.

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<sup>517</sup> Decree 49, article 17.

<sup>518</sup> See *supra* Sections 2.3.1 and 3.4.2.

<sup>519</sup> *Supra* Section 2.5 and *supra* n.160 and *infra* n.859 and 912.

<sup>520</sup> Decree 49, article 15.



If the joint enterprise did not have the right of ownership, the property contributed to it would have remained in the direct ownership of its participants, or in the case of the Soviet participant, would have remained in state ownership (as it was allocated to the Soviet participant by the state for operative management only). Consistent with this approach was the right of a foreign participant to withdraw from the joint enterprise and the consequential "right of *return* of its contribution (*"vozrat svego vklad"*)".<sup>521</sup> Not only does the reference to "return" imply that ownership was never transferred, but also the right of withdrawal was contemplated in the law of common ownership.

Although a number of schools of thought emerged relating to the question of joint enterprises and the right of ownership,<sup>522</sup> as discussed in the previous Section of this study, the logic of understanding the ownership question within the framework of existing Soviet law is inescapable. First, the absence of the right of ownership of a joint enterprise notionally preserved the principle of state ownership of the means of production, as state property contributed to the joint enterprise would have still remained in state ownership. Furthermore, the Soviet law on ownership was based on the identity principle. The law was not concerned with developing a legal regime for fragmented ownership on the basis of ownership interests of juridical persons. As such, the terminology of Decree 49 was only confusing when forced to answer a question that the legislation was never designed to tackle (ie who owned the joint enterprise?). The logic of the Soviet law on ownership was aimed only at identifying "exceptions" to the state ownership regime on the basis of forms of ownership. Clearly the joint enterprise did not fall within one of the existing exceptions and equally clearly it was not provided in Decree 49 as constituting an additional new exception. Hence it had no right of ownership.

Unfortunately, while this regime made sense within the logic of the socialist, quasi-feudal, law on ownership, it was entirely anachronistic for the purposes of regulating in practice a body corporate with fragmented ownership. The function of the joint enterprise was quite different from the function of the state enterprise and this change in function necessitated a change in law and theory. And so the systemic flaw within the Soviet law of juridical persons, the absence of an understanding of the concept of the ownership interest, condemned the joint enterprise to an uncertain foundation. For Soviet law to break loose from its socialist heritage,

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<sup>521</sup> Decree 49, article 51 [emphasis added].

<sup>522</sup> These included the following theories: the joint enterprise did have the right of ownership; the state owned the property and transferred it to the joint enterprise to be held by way of a right akin to operative management; ownership was based on some kind of fiduciary concept (*"fidutsiarnaya sobstvennost"*); or there was some kind of separation of ownership (*"rasshcheplennaya sobstvennost"*) (see supra n.431, pp.42-47).



it would have to re-evaluate fundamentally the structure of its ownership law and reorientate the classification and understanding of juridical persons towards a concept based not on identity, but on ownership interests. Only in that way could the Soviet, or feudal, identity principle be avoided, and with it analysis like that of Golubov when he concluded that "we must recognise joint ventures as Soviet legal entities, with Soviet law as their personal law. This is at any rate apparent when the overall participatory share of the Soviet side in the capital fund is over 50 per cent".<sup>523</sup> For it is a curiosity of socialist law that fixes the nature and classification of the juridical person by reference to the *identity* of its owners.<sup>524</sup>

#### 5.4.3 *The Operation of the Board and the Directorate - Governance Regime and Management*

The provisions of Decree 49 relating to internal governance were extremely brief and consisted of one single article (article 21) comprised originally of four brief sentences.

The brevity with which Decree 49 dispensed with the issue of internal governance indicated again that the joint enterprise was a product of mainstream Soviet understandings: the rationale of legislation was to protect the state and this was achieved through the concession and authorisation process and other mandatory requirements in Decree 49. As the state was no longer directly the creator-owner, it was less concerned with the nature of the contractual arrangement as agreed between the participants on the question of governance. Furthermore, Soviet law did not have a tradition of detailed procedural governance frameworks: the industrial juridical person was based on the principle of one-man management and in that context complex governance rules were simply not necessary. As has been suggested above, the Soviet regime did not fully grasp the significance of the joint enterprise as a juridical person based on fragmented ownership and therefore its challenge to the existing legal civil law structures. The rudimentary provisions on governance further reflected this myopia.

The legislation did however take two important and fundamental steps. First, it recognised the beginnings of the separation of ownership from control and therefore provided for two bodies, a board (the higher organ) consisting of representatives of the participants, and the directorate (the executive organ) that controlled operations on a day-to-day basis.<sup>525</sup> Secondly, for the first time in relation to a Soviet industrial juridical person since the 1920s, the Model Charter did provide some further detail on the rules and procedures for internal governance and these

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<sup>523</sup> Ibid., p.11.

<sup>524</sup> Infra Sections 7.2 and 7.4.2.1.

<sup>525</sup> In addition, Decree 49, article 44 contemplated the possibility of creating an audit commission (the control organ).



seemed to be indebted both to collective farm charters (as collective farms always had had collective decision making bodies) and the charters of the international joint ventures with members of SEV.

Despite the brevity of article 21 and hence the increased scope for "contracting" in relation to governance procedures, the legislation did provide some mandatory rules: The head of the board was the chairman, and the head of the directorate was the managing director. Initially Decree 49 provided that both posts had to be filled by citizens of the USSR.<sup>526</sup> Like other mandatory rules, this requirement was removed by Decree 385 which stated that a foreign citizen could hold either, but only one, of the two posts. In addition, Decree 385 required that "principal questions of the activities" of the joint enterprise must be decided at sessions of the board by a unanimous vote. However Decree 385 was silent as to which issues constituted "a principal question". Once again this was elaborated in the charter and subordinate legislation.

The Model Charter did provide more detail on these governance issues and in particular included "directions" which were reminiscent of the coercive law of the confirmation model. Thus article 5 of the Model Charter provided that each participant had the obligation "to make contributions...to the charter fund in accordance with this Charter and resolutions of the superior organ of the enterprise" and that late payments would be subject to a 3% per annum interest amount in accordance with the civil codes.<sup>527</sup> In addition, article 5 provided that the participants had an obligation "to participate in the management of the enterprise". Professor Braginskii explained that "participation in management is primarily the right of a member of a joint economic organisation. Additionally, the member of the joint economic organisation is *obliged* at the same time to participate in the management...[because] passive conduct of the participants may paralyse the organization's activities, so far as a refusal to participate in the work of the superior organ makes it practically impossible to adopt resolutions important for its operation, in particular, those which require unanimity".<sup>528</sup> Therefore, rather than leaving systemic and economic mechanisms to incentivise participation, Braginskii noted that this was also required by coercive diktat.

Despite the role of the Model Charter in providing supplementary provisions, Decree 49 essentially left the elaboration of the governance regime up to contract. It seems as if the state was more interested in protecting "its" position rather than developing a sensible internal

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<sup>526</sup> Decree 49, article 21. Interestingly (and symptomatic of the identity principle) Decree 49 did not specify which participant should appoint them, but merely the identity of their nationality.

<sup>527</sup> RSFSR CC, article 226.

<sup>528</sup> Supra n.397, p.70.



governance system for a body corporate with fragmented ownership. The legislation was aimed at protecting the interests of the state. This could not have been achieved through the internal governance regime as the state was no longer the sole and direct owner of the joint enterprise and was no longer part of the voting mechanism. As a consequence, the participants were left free to negotiate the terms of their cooperation and governance based on their relative negotiating strengths (and of course the Soviet participant implicitly had as an ally the superior state organ which had to approve the constitutive documents). Mandatory rules for governance, including for the protection of minority shareholders, were simply absent and were, like the ownership interest, overlooked as logic of the command economy, the legacy of the confirmation model, and the Soviet forms of ownership, prevailed.

### 5.5 Joint Enterprise - Enterprise or Corporation?

This Chapter has traced the development of a new form of juridical person based on a retreat by the state from its "traditional" role as creator-owner, and arguably from its role as property-owner. If not doctrinally, then at least in practice, an exception was created to the general rule of state ownership of the means of production with the introduction of the right of third persons to create Soviet industrial organisations. The state was required to rely on legal mechanisms to protect its interests through the concession procedures. The participants could then rely on contract to elaborate and protect their rights against one another, and against the directorate. While this model radically departs in these fundamental respects from the confirmation model, the question as to whether both models gave rise, in conceptual terms, to an "enterprise" has so far been avoided. Purely as a matter of terminology, the prevailing Soviet legislation referred to both the confirmation enterprises and to the contract-based concession enterprise as "enterprises" ("*predpriyatie*"). The question is whether this was a coherent and consistent use of the term.

It shall be argued that this terminology was correct, and for this reason, the term "enterprise" has been retained in the descriptions of both models. In particular, the Soviet concept of "the enterprise" has to be distinguished from the concept of "the corporation". The difference between the enterprise and the corporation is, in this context, best understood by reference to the Soviet law on ownership. The enterprise was a traditionally Soviet concept and a product of an essentially Soviet economy. As was outlined in Chapter 2, the law on ownership looked to establish the fundamental principle of state ownership of the means of production and set out the identity of specific persons that were exceptions to this rule. The economy was then elaborated on the basis of state control of the means of production through the state plan. As was argued in Chapter 3, the industrial enterprise was born of the need to preserve state ownership of the means of production while providing for a separated subject of civil law that



could act as the addressee of the plan, with a separate balance sheet that enabled its economic "performance" to be assessed individually. So the Soviet "enterprise" evolved as a product of this ownership regime existing as an indivisible object of the law on ownership, with a single owner and incapable of owning property in its own right.

The joint enterprise posed a singularly unique problem within the context of the Soviet law on ownership. The Brezhnev Constitution did not contemplate a "form of ownership" for an industrial juridical person owned by a person other than the state: Ownership by a joint enterprise neither constituted state ownership, collective farm-cooperative ownership nor personal ownership. Moreover, Soviet law in general did not contemplate multiple owners of an industrial organisation. Hence, in this context, it had no understanding of the nature of the ownership interest, no precedent for dispute resolution between participants through internal governance structures, and no understanding of the nature of the relationship between different owners and the juridical person. As such, the mere existence of the joint enterprise forced a reassessment of the ownership regime at the heart of Soviet civil law as established by Venediktov in the 1930s.

There were three alternatives.

First, to ignore this challenge by continuing to regulate this juridical person within existing Soviet law theory and to ignore the theoretical problems raised by fragmented ownership through de-emphasising its role as a domestic juridical person and by characterising it essentially as a vehicle for foreign relations law.

Secondly, to amend the existing law on ownership to contemplate a further exception to the principle of state ownership of the means of production (ie to give the joint enterprise the right of ownership).

Thirdly, to recognise that forms of ownership as a theoretical framework for the classification and regulation of associations and property rights was anachronistic in the context of these new industrial organisations and to develop a law suitable for the regulation of organisations with fragmented owners providing investment capital.

It is only through the adoption of the third path that a corporation could have emerged: a juridical person operating in a regime of multiple owners unrestricted by their identity, with developed rules for internal governance organs and procedures, based on an association of



capital where ownership by the participants of ownership interests of a juridical person was separated from ownership by that juridical person itself.<sup>529</sup>

As it was, Decree 49 opted for the first path and de-emphasised the "ownership problem". The analysis presented in this Chapter, and latent in the drafting of the legislation, was never explicitly developed in any of the Soviet law textbooks or treatises which generally overlooked the issue or merely touched upon it as an uncertain area. While in practice the challenge to existing principles prevailed, the traditional Soviet "enterprise" as an object of the law on ownership, bereft of the right of ownership, and founded upon an ownership framework structured by reference to the identity of the owner, was for the time being preserved.

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See *infra* Section 7.2 *et seq.*



6      **MODEL 3 - THE PARTICIPATION ENTERPRISES (1987-1990): 1987 STATE ENTERPRISES, 1988 COOPERATIVE ENTERPRISES AND 1989 LEASED ENTERPRISES**

*"In proletarian nationalisation, obversely, the workers in the separate factories lose nothing by the fact that they are not independent masters in their own factories, by the fact that all the enterprises belong to the working class in its entirety, to the greatest of all workers' organisations, which is known as the Soviet State."*

N. Bukharin and E. Preobrazhensky

The first years after Gorbachev's appointment as General Secretary were characterised by a number of initiatives that picked up where Andropov's reforms had left off. These included measures on tackling corruption and alcoholism, and increasing labour discipline.<sup>530</sup> The replacement of the gerontocratic bureaucracy of the Brezhnev state continued apace. The basic assumption was still that state planning was the most efficient framework for the Soviet industrial economy but that the Stalin centralised "command" form of that economy had to be "restructured" in a way so as to incentivise the workforce and "activate the human factor". Towards the end of 1986 this developed into a call for greater democracy and openness ("*glasnost*") and with it came the possibility for individuals to exercise increasing autonomy both in political and economic life. The Law on Individual Labour Activity of November 1986 provided a limited legal regime for the carrying out of small scale entrepreneurship - an activity that had been prohibited and pushed "underground" since the early 1930s. Gorbachev, in his keynote speech on *perestroika* to the January 1987 plenum, expressly called for steps "to deepen socialist democratism and to develop self-management of the people".<sup>531</sup> In a striking parallel with the NEP era initiatives, the touchstones again were discipline, responsibility and incentivisation.

The Gorbachev reforms first attempted to "remedy the glaring flaws of the system...within the traditional framework, without venturing to encroach upon the fundamentals of the

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<sup>530</sup> See Richard Sakwa, *Gorbachev and His Reforms, 1985-1990* (Prentise Hall:1990), pp.65-125.

<sup>531</sup> O Perestroike i Kadrovoi Politike Partii, Doklad na Plenum TsK KPSS, 27 Yanvarya 1987, 4 IRS 299, at p.316



Communist faith",<sup>532</sup> before moving on to embrace the principles of democratisation and *glasnost* in an attempt "to wake up those people who had fallen asleep".<sup>533</sup> It was however only later, in what Gorbachev called "the third period from 1990 to 1991",<sup>534</sup> that the actual basic tenets of the planned economy themselves came to be questioned. Until then, Gorbachev persisted with policies aimed at perfecting state planning through encouraging greater participation by the workforce and through increasing decentralisation. As Gorbachev explained, it was imperative "to use the advantages of the planned development of the socialist economy - that is our approach. Not the market, not the anarchic forces, but above all the plan must determine the basic features for the development of the national economy. At the same time we must carry out new approaches to planning, to actively adopt economic levers, to give more scope for initiatives for the labour collectives".<sup>535</sup>

This whirlwind environment of the *perestroika* years to 1990 gave rise to a number of seemingly unconnected organisational forms introduced into the industrial economy, including the 1987 state enterprises, the 1988 cooperative enterprises, and the 1989 leased enterprises. Each was created pursuant to discrete legislation (respectively, the State Enterprise Law, the Cooperatives Law and the FP Lease) and each was presented as a separate initiative on the road to further perfecting the socialist economy. On the face of the legislation, each of these forms appeared as structurally quite different. However, it shall be argued in this Chapter that all of these enterprises were born from within a single unifying policy and were based on common principles underlying their organisational role and operation.

The overarching model for the enterprises of this period has been called the "participation model". This is for two reasons. First, in this model, the single and central role of the state has been supplemented by a new interest, that of the "participant". Secondly, the notion of "participation" was chosen because each of these enterprises seemed to emerge from a policy of attempting to ensure "personal participation" in the organisational forum. Participants were not to be silent holders of equity-like ownership interests, providers of capital, without any further role. Instead, their very presence was premised upon their direct involvement in the day-to-day business of the enterprises. If the contract-based concession enterprises radicalised the "contract" element of the contract for joint activity, the participation enterprises took this a stage further by radicalising the "joint activity" element.

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<sup>532</sup> Mikhail Gorbachev, *Memoirs* (Doubleday:1996), p.569.

<sup>533</sup> Mikhail Gorbachev, *Perestroika, New Thinking For Our Country and the World* (Collins:1987), p.29.

<sup>534</sup> Supra n.533.

<sup>535</sup> Reshitel'no Provodut' Namechennyi Kurs, Rech' v Gorode Kieve na Sobranii Aktiva Respublikanskoi Partiinoi Organizatsii Ukrainy, 27 Iyunya 1985, 2 *IRS* 303, at p.317.



Personal participation was primarily to be achieved by three methods: the first two were rooted in the principles of the then current stage of *perestroika*, and the third was based on a traditionally Soviet technique.

***The Three Pillars of the Participation Model*** Participation was promoted:

1. by introducing economic incentives which gave the participants a stake in the profitability of the enterprise (ie linking their wages to the amount of the residual profit - this was distributed between the participants in accordance with their labour contributions);
2. by giving the participants some control over the activities of the enterprise and hence control over its profitability (ie democratisation - giving the participants rights in the management of the enterprise); and
3. through the traditional "Soviet" technique of legislative coercion (ie directing the participants to act in a particular way through legislative diktat).<sup>536</sup>

***Theoretical Imperatives of the Participation Model*** These "three pillars" of the participation model were founded upon two underlying theoretical imperatives, both of which were again derived from the general trend of the *perestroika* reforms to 1990:

- (i) The first was the preservation of the Stalin spine of state ownership and control of the means of production coupled with state planning.<sup>537</sup> This imperative therefore required a legal framework rooted in the existing Soviet law on ownership.
- (ii) The second was the development of the concept of the "interest of the participant" as separate and distinct from that of the state.

Traditionally, within the Soviet industrial economy and within the confirmation model there had been no acknowledgement, or possibility for, the existence of any "interests" separate from the interests of the state. The creation of an "all-people's state" was declared in the 1961 Party Programme,<sup>538</sup> and this was then reiterated in the preamble to the Brezhnev Constitution adopted in October 1977.<sup>539</sup> Therefore in accordance with the then prevailing ideology, the Soviet state (as directed and guided by the Communist Party) represented the interests of all

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<sup>536</sup> Examples of this third method can be seen in the confirmation model, supra Section 3.4.3.

<sup>537</sup> On the Stalin economic settlement, supra Section 2.2.

<sup>538</sup> *Istoriya Kommunisticheskoi Partii Sovetskogo Soyuz* (Izdatel'stvo Politicheskoi Literatury:1980), p.593.

<sup>539</sup> The preamble acknowledged that the Soviet Union had reached the stage of "a developed socialist society" with the establishment of a "socialist all-people's state": the class conflict of the 1920s and 1930s was declared to be finally at an end; and the defeat of "the power of the capitalists and landowners" and the "coming together" ("*sbliizhenie*") of the working class, collective farm peasantry, and intelligentsia had created a "socio-political unity" embodied by the concept of the "socialist all-people's state".



Soviet people and as such there was no need for dissent or discussion, nor any need for interest groups to debate policies in a democratic forum. Consequently, there was no admission of the presence of different "interests" in the confirmation model, either within the organisational forum or external to it. Internally, the state, the one-man manager and the workforce were treated as having a coincidence of interests and the crude governance system of the confirmation model in part reflected, and in part reinforced, that fact. Externally, there was no developed law of "ownership interests" because all industrial enterprises were owned entirely by the state and as such were treated as indivisible objects located "in" state ownership.<sup>540</sup>

During the *perestroika* years, the concept of a person as having an interest separate from that of the state was first implicitly developed in the legislation giving rise to the contract-based concession enterprises (ie Decree 49).<sup>541</sup> However, these joint enterprises presented a very different framework particularly because the separate interest was "foreign" and therefore did not conceptually entail the fragmentation of the Soviet all-people's state. By contrast, the participation model transported this concept of "interest" directly into Soviet domestic economic relations thereby enabling the development and official recognition of the possibility for incentivising interests separate from that of the state - ie the interests of participants.

The development of a fragmentation of interests was never mentioned expressly in the State Enterprise Law; however it shall be argued that it was implicit throughout. 1987 state enterprises, the first expression of the participation model, then gave way to more complex expressions, particularly in the form of the 1988 cooperatives and the 1989 leased enterprises, which consolidated the concept of "separate interests" and further developed the three pillars of the participation model. These later expressions each began to erode the features of the governance regime of the confirmation model. In this way it shall be argued that the notion of the separate interest of the participant (ie the second theoretical imperative of the participation model) contained the seeds of the destruction of the socialist state owned economy (ie the first theoretical imperative of the participation model). An economy based on different interests pursuing independent goals, premised upon a quasi hidden hand analysis, is broadly mutually exclusive to one based on a single interest "required" to be pursued by all components of a planned economy.

In the final expression of this model, the leased enterprise, the dynamic of the participation model and the separation of interests is pushed to its logical conclusion, resulting in the

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<sup>540</sup> Supra Sections 2.3.1 and 2.5.

<sup>541</sup> Supra Section 5.1.



complete dismantling of the confirmation governance regime. Furthermore, this expression occasioned a change to the nature of the juridical person itself, from one conceived of as an indivisible object, to an organisation constructed by contract and bound by the rules of civil law.

## 6.1 Foundations and Basic Principles of the Participation Enterprises

Unlike the organisational forms introduced after 1990, including joint-stock societies and partnerships, the participation enterprises were developed from within traditional aspects of mainstream Soviet law of the time. The state enterprise, the cooperative and the lease contract were all features of the prevailing legal system, as was the notion of participation. The participation enterprises did not therefore constitute a revolution of the planned economy but, to borrow the term from Garton Ash, should be regarded as a "refolution".<sup>542</sup> In the years to June 1990 there was no intention to dismantle the socialist nature of Soviet industrial organisations nor the pervasiveness of state power, but merely an attempt to "refolute" existing structures from within, to "further perfect" existing mechanisms and to improve productivity, quality, initiative, incentives, technological renewal and large scale investment. It was only the unintended consequences of this model, and in particular the fragmentation of the concept of the all-people's state, that was to lead to genuine "revolution" or more accurately, to the possibility of one, in June 1990.

### 6.1.1 General Theoretical Foundations - Constitutional and Collective Farm Law

On the basis of the declaration of the "all-people's state", Chapter 1, Section I of the Brezhnev Constitution included provisions on ensuring the protection of the legal order, the interests of society and the rights and freedoms of citizens. While much attention at the time of its adoption was focused on article 6 of this Chapter,<sup>543</sup> the Brezhnev Constitution contained three additional articles in this Chapter that were not present in the former Stalin Constitution. The constitutional foundations of the duty to participate, and hence the basis for the participation model, can be traced to these articles.<sup>544</sup> Article 7 provided that "trade unions...*cooperatives* and other social organisations in accordance with their charter tasks shall *participate* in the administration of state and social affairs and in the deciding of

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<sup>542</sup> A midpoint between "reform" and "revolution". Timothy Garton Ash, *The Uses of Adversity - Essays on the Fate of Central Europe* (Granta Books:1989), p.276.

<sup>543</sup> Article 6 provided that the Communist Party was the "guiding and directing force of Soviet society". It thus elevated the Communist Party to a constitutional status which had previously been absent in the Stalin Constitution.

<sup>544</sup> Emphasis has been added in the translation of each of the following extracts of the articles of the Brezhnev Constitution.



political, economic and socio-cultural questions"; article 8 then continued, "*Labour collectives shall participate* in the discussion and deciding of state and social affairs, in the planning of production and social development...and in the discussion and deciding of questions of the management of enterprises and institutions...and also for socio-cultural measures and material incentive. Labour collectives shall develop socialist competition, promote the dissemination of progressive work methods and the strengthening of labour discipline...";<sup>545</sup> and article 9 finally reaffirmed the general principle of "socialist democracy" as "the basic orientation for the development of the political system...more extensive *participation* of citizens in the administration of the affairs of the state...intensifying people's control...and constantly taking account of public opinion".

By setting out the ways in which the cooperative, the labour collective and the citizen were to participate in the political system, these constitutional provisions provided the theoretical basis for the "democratisation of the workplace" that formed a central pillar of the participation model. Moreover, they hinted at the *identity* of the participant for each of the three expressions of this model - the cooperative or citizen as in the cooperative enterprise; the labour collective as in the state enterprise; and the citizen or labour collective as in the leased enterprise.

In addition to participation and democracy, the other pillars, namely economic incentivisation and coercive law, were also present in the Brezhnev Constitution. Article 40 provided for the right of citizens to work and to receive payment in accordance with quantity and quality of work done and article 60 provided that it was "the duty and honour for every citizen" to engage in "conscientious labour...and observance of labour discipline". What of course the Brezhnev Constitution did not recognise was that deepening democratisation and incentivisation would in practice lead necessarily to a questioning of the very concepts upon which the Soviet state was built - the abolition of class conflict in the USSR; central planning; the all-people's state; and the coincidence of interest between the state and the citizen.

The concept of the interests of the participant as separate from those of the state, and the three pillars of democracy, incentivisation and coercive law were not only latent in the provisions of the Brezhnev Constitution, but were also contemplated by the prevailing law on collective farms, the principal form of juridical person in the agrarian economy.

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<sup>545</sup> A commentary to the Brezhnev Constitution noted that article 8 setting out the rights of the labour collectives was, in an earlier draft of the constitution, placed in Chapter 2 on the Economic System; however it was moved by the Constitutional Drafting Commission to Chapter 1 on the Political System "to reflect the participation of the labour collective in political life" (supra n.93, p.45).



The need to balance social (ie state) interests with personal interests (ie those of the collective farmer (or the *dvor*)) developed out of the history of collectivisation between 1929 and 1935.<sup>546</sup> What emerged was a settlement that conceded certain formal legal rights to the collective farmers (ie the participants). Thus (i) the collective farm of 1935 took the form of the *artel* which had the right of ownership (cooperative-collective farm ownership) separate from state ownership; (ii) collective farmers were paid in accordance with the quality and quantity of their work, with the right to dispose freely of excess production (incentivisation); (iii) collective farmers had the right to participate in general meetings of the management of the farm (collective farm democracy); and (iv) collective farmers retained the right to farm subsidiary personal plots side-by-side with those of the collective farm. The state was left to protect its interests principally through coercion using its roles as legal and economic sovereign (by respectively promulgating laws and issuing "administrative" instructions).

The law of the industrial economy was not burdened by the need to legitimate the history of collectivisation and therefore gave rise to organisations with a stricter, more direct, state governance regime which ensured state control through overlapping mechanisms where even the formal legal rights of the participants (ie the workers) were extremely limited.

The participation model adjusted the traditional governance framework of these industrial confirmation enterprises and incorporated elements of the collective farm compromise as well as the constitutional principles expressing the importance of "participation", including the twin pillars of incentivisation and democracy.

It may have been Gorbachev's early career in the party that led him towards transporting certain aspects of the agricultural organisational model into the industrial economy. Gorbachev had considerable direct experience with the Soviet agricultural settlement (both its law and in practice). He was by training a lawyer and was appointed to the post of first secretary of the agricultural province of Stavropol in 1966. In 1978 he was promoted to the Party secretariat in Moscow in charge of agriculture.

Indeed the pillars of incentivisation and democracy can be traced not only to collective farm law generally, but also, more specifically, to Gorbachev's initiatives in Stavropol in the early 1970s. He introduced the "team contract" system where small teams or brigades were allocated land, materials and resources and were allowed relative freedom to organise their

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<sup>546</sup>

Supra Section 2.4.1 and infra Section 6.1.3.



labour and were paid by results.<sup>547</sup> Gorbachev later returned to the issue of incentivisation in his memorandum of May 1978 (published only after he became general secretary) where he suggested that "administrative methods" would not achieve the necessary increase in productivity and that "material and moral stimulation" was needed - "most principally, most importantly, in our opinion, is to reconstruct a mechanism of economic stimulation of agricultural production under the combination of general state interests with the interests of collective farms and specific workers in agriculture...".<sup>548</sup> Gorbachev again stressed the role of the agricultural model in October 1987 when in his book, "*Perestroika*", he referred directly to the advantages of building industrial organisational models from within the "agro-industrial complex". He explained: "for one thing, our collective farms have long-standing traditions. For another, rural folk are enterprising and resourceful. All this makes for greater social mobility and flexibility when applying cost-accounting, self sufficiency and self-financing".<sup>549</sup>

The influence of the principles of collective farm law in the legislation on the participation enterprises will be illustrated throughout this Chapter. Most obviously the Cooperatives Law, as well as introducing a "new" organisation into the industrial economy, also provided a new basis for collective farm legislation as a whole.<sup>550</sup> And so, while the participation model posed a threat to the organisation of industry as conceived within the confirmation model, its basic tenets had been for some time latent in the Brezhnev Constitution and in the collective farm law of the parallel, but separate, agrarian sector of the Soviet economy.

### 6.1.2 1987 State Enterprises

It was understandable why the Soviet regime looked to state enterprises and associations as the starting point for the development of the participation model in practice. The state enterprise was the principal organisation within the industrial economy and if the confirmation model could have been adjusted to produce the required efficiency gains, without prejudicing the existing external structure of the national economy, then this clearly would have been the most uncontroversial policy.

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<sup>547</sup> Angus Roxburgh, *The Second Russian Revolution - The struggle for power in the Kremlin* (BBC Books:1991), p.12. In 1983 the Politburo permitted Gorbachev to continue with the collective contract system in agriculture, linking wages to productivity (see, *Pravda* 20 March 1983).

<sup>548</sup> O Nekotorykh Merakh Posledovatel'nogo Osushchestvleniya Agrarnoi Politiki KPSS na Sovremennom Etape, iz zapiski v TsK KPSS, Mai 1987, 1 *IRS* 180, at p.184.

<sup>549</sup> Supra n.533, p.96

<sup>550</sup> As the collective farm was a type of "cooperative", it fell within the framework of the Cooperatives Law and indeed the adoption of the Cooperatives Law was accompanied by the enactment of a new 1988 Model Charter.



The State Enterprise Law was adopted in a blaze of legislation in June 1987. Following the June 1987 Plenum of the CPSU and the 11<sup>th</sup> Congress of the 7<sup>th</sup> Session of the Supreme Soviet, three laws were adopted.<sup>551</sup> Specific aspects of these laws were then developed in greater detail in thirteen decrees enacted at the same time.<sup>552</sup>

The form of the State Enterprise Law was to set the trend for all the primary laws on the participation enterprises. First it was extremely long, covering some 25 articles with each generally having at least 4 sub-articles. Secondly, it was drafted by committee following public comment. A draft was published for discussion in February 1987.<sup>553</sup> In the process of finalising the law prior to its enactment, more than 140,000 suggestions and comments were submitted and considered.<sup>554</sup> Thirdly, the State Enterprise Law was the first time in the Soviet period that "a law" ("*zakon*") had been adopted in connection with a single industrial organisation. In the past, industrial organisations had operated on the basis of statutes or decrees (a lesser form of legislation). The status of a "*zakon*" indicated the overall importance of this policy initiative. Fourthly, this law regulated both the enterprise and the association, and therefore unified the treatment and approach to two functionally similar entities that had previously been regulated by different statutes.<sup>555</sup> Finally, the drafting and detail of the legislation gave the impression of a state "feeling its way". From reading the State Enterprise Law, it is difficult to understand exactly how many of the provisions were intended to operate in practice. There were numerous lists that read like a manifesto, setting out programmatic intentions and consequence. There were many basic principles but few detailed rules. This was in part a reflection of the legacy of coercive law: directions of obligations set out in list form. However the legislation on the participation enterprises went beyond mere coercion, and the drafting seemed to betray the fact that the legislator was almost searching for solutions to economic problems by tinkering and by stating broad policy statements, without looking closer at how these were to be implemented in practice. And therefore much of this legislation was imprecise, contradictory and reflected the inevitable tensions between the desire to retain

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<sup>551</sup> The State Enterprise Law; the Law on All People Discussion of Important Questions of State Life; and the Law on the Procedure for the Appeal to Court of Illegal Actions of Officials Encroaching upon the Rights of Citizens.

<sup>552</sup> See *Zakonodatel'stvo o Korennoi Perestroike Upravleniya Ekonomikoi* (Yuridicheskaya Literatura:1988) for a collection of these three laws and the thirteen decrees of 17<sup>th</sup> and 30<sup>th</sup> June.

<sup>553</sup> See *Pravda* and *Izvestiia* (8 February 1987).

<sup>554</sup> Supra n.552, p.3.

<sup>555</sup> The Enterprise Statute and the Production Association Statute. This functional similarity is recognised in the confirmation model which is intended to be applied in understanding the legal framework of both organisations.



as much of the framework of the existing planned economy and legal structure of ownership relations as possible, while satisfying the need to encourage real participation.

In terms of substance, the traditional view of the State Enterprise Law was described by Feldbrugge: "most of its progressive sounding innovations were counterweighed by the retention of traditional mechanisms. Prices remained centrally controlled; the enterprise conducted its own planning, but its plans had to incorporate state orders (*goszakazy*); the director was to be elected by personnel, but needed confirmation from above. The Law, in short, was a damp squib...[and] yielded almost no positive results."<sup>556</sup> It was clearly intended that the "new" 1987 state enterprises would operate broadly within the planned economy, however this did not mean that there were "almost no positive results". Feldbrugge ignored perhaps the principal significance of the State Enterprise Law. This was not stated explicitly in the positive provisions of the law but could only have been derived from the theoretical implications that lay beneath those provisions. Within domestic Soviet law, the State Enterprise Law took the first radical step away from the confirmation model, towards a new organisational strategy based on the role and importance of the participant, which, when developed to its logical conclusion, posed an inescapable dilemma in relation to state governance, not just of industrial organisations themselves, but of the national economy as a whole. The contribution of the State Enterprise Law in the development of the industrial organisation during the *perestroika* years lay not in the way it changed the relationship between the enterprise and the state (for state planning and state orders still remained); nor in terms of altering the scope of the state's roles in the basic governance system (for state ownership of the enterprise, its property and the state's roles as legal and economic sovereign remained); but in the acknowledgement that there were deep systemic economic, incentivisation and democratic problems at the heart of the existing structure of Soviet confirmation enterprises that could only be overcome by recognising the separate interest of "the human factor"; an interest that was independent from that of the state as a whole, and that needed to be activated in order to make the industrial organisation a more efficient unit in a coordinated national economy capable of reproduction and development.

For the purposes of the participation model, the relevant "participant" within the State Enterprise Law was the "labour collective". The participatory role of the labour collective was specifically mentioned in the Brezhnev Constitution,<sup>557</sup> and its importance had been recently

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<sup>556</sup> Supra n.34, p.59 and p.252.

<sup>557</sup> Supra Section 6.1.1.



acknowledged in Andropov's Law on Labour Collectives of 1983.<sup>558</sup> This 1983 law attempted to give members of the collective (either directly, or through the general meeting (conference) of the labour collective) increased participation in formulating the overall direction of the activities of the enterprise, including matters connected with pay, labour discipline and protection of labour. However its purpose seemed to be more about improving efficiency than about creating a genuine workers' democracy.

Gorbachev, following his appointment as General Secretary, was quick to assert the key role of the labour collective. Decree 669 "On Extending the Application of New Methods of Economic Mechanisms and Strengthening their Influence on the Acceleration of Scientific-Technical Progress" dating to July 1985 acknowledged, in the context of developing new economic conditions, the necessity of ensuring the "interestedness of the labour collective";<sup>559</sup> and out of the three sections in each decree enacted during 1985 and 1986 to implement Decree 669, one entire section was devoted to "Increasing the Interestedness of the Labour Collective in the Growth of Efficient Production and Strengthening *Khozraschet*".<sup>560</sup> Gorbachev again returned to the importance of the labour collective and its participation and interestedness in the results of their work in his speech to the XXVII Congress in February 1986 where he noted that "in the use of social ownership it is necessary to raise decisively the role of the labour collective."<sup>561</sup> On the basis of the decisions of the XXVII Party Congress, the decrees enacted during the course of 1986 aimed at transferring enterprises and associations within various Ministries to full *khozraschet* also contained a section on increasing the interestedness of the labour collective in broadly similar terms to those decrees implementing Decree 669.<sup>562</sup>

Although the State Enterprise Law continued and radicalised this trend of passing control to the labour collective, this was intended only as a measure to be developed within a socialist framework. Therefore while the preamble to the State Enterprise Law referred to the two

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<sup>558</sup> O Trudovykh Kollektivakh i Povyshenii ikh Roli v Upravlenii Predpriyatiyami, Uchrezhdeniyami, Organizatsiyami, *Vedomosti SSSR* (1983), no.25, item 382.

<sup>559</sup> O Shirokom Rasprostranении Novykh Metodov Khozyaistvovaniya i Uselenii ikh Vozdeistviya na Uskorenie Nauchno-Tekhnicheskogo Progressa, *Postanovleniya* (July 1985), no.669, p.198.

<sup>560</sup> Unfortunately none of the implementing decrees of 1985 and 1986 were published in the official gazette (*SP SSSR*). For references and further discussion of these decrees, see infra Section 6.3.2.

<sup>561</sup> *XXVII S'ezd Kommunisticheskoi Partii Sovetskogo Soyuza - Stenograficheski Otchet - 1* (Izdatel'stvo Politicheskoi Literaturi:1986), p.61.

<sup>562</sup> Supra n.560.



principal pillars of the participation model (democratisation,<sup>563</sup> and incentivisation<sup>564</sup>), it then set out the parameters for their operation in practice, noting that the present law shall "determine the economic and legal basis of the economic activities of the *socialist* state enterprises...strengthen state (all-people's) ownership of the means of production...deepen the centralising principles in the resolution of important tasks of the development of the national economic as a single unit".<sup>565</sup> This was then developed in the article 1 definition of the state enterprise as a "socialist goods producer" whose principal role was in the achievement of the "supreme goal of social production under socialism".<sup>566</sup>

Despite its professed socialist orientation and its aim of strengthening state ownership within the context of a planned *unified* national economy, the State Enterprise Law can be viewed as the first expression of a distinct and new model. It developed the concept of the interest of the participant, as separate from that of the state, and therefore held out the possibility of a fragmented economy founded upon different interests. It introduced incentives in an attempt to activate the participant's interest and developed a democratic internal structure to enable that interest to be voiced. Finally, the state began to reorientate its governance regime toward legal methods, principally based on legislative diktat. The 1988 cooperatives then built upon the steps taken by the 1987 state enterprises by moving the concept of participation from a state-owned juridical person, to one that was no longer state owned.

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<sup>563</sup> The law "shall broaden the possibility of participation of labour collectives in the effective use of its property, in the management of the enterprises and associations, in the deciding of state and social affairs...".

<sup>564</sup> The law "shall provide for the strengthening of economic methods of management, the use of full *khozraschet* and self-financing, broaden the democratic basis and development of self-management".

<sup>565</sup> Emphasis added. Interestingly the word "socialist" in this quotation from the preamble was not in the February draft law but was added following subsequent discussions.

<sup>566</sup> Further references to the socialist system and the role of the party were made at various other places throughout the State Enterprise Law.

On the socialist system, see for example, references to: "the principle of socialist self-management" (article 2(3)) and "centralised management and socialist self-management" (article 6(1)); the planned economy (infra Section 6.3.4.4) and state ownership (infra Section 6.3.4.3); "socialist legality" (article 2(5)); and cooperation with socialist countries (article 19(2)).

On the role of the party, see for example, references to: its role generally in state planning (article 2(1)); the "party organisation, as the political core of the labour collective" (article 6(1)); the right of the party to submit questions to the meeting of the labour collective (article 6(6)); its role in confirming the conditions for socialist competition (article 7(1)); the right of party representatives to be elected to the collective council (article 7(3)); and its role in the placement and selection of personnel (article 8(1)).



### 6.1.3 1988 Cooperative Enterprises

The attempt to develop the industrial organisation by looking to "refoliate" organisations already present within the mainstream Soviet economy broadened with the adoption of the 1988 Cooperatives Law. Cooperatives, like state enterprises, were a key existing part of the national economy. The Brezhnev Constitution, the State Enterprise Law and the Cooperatives Law all conceived the national economy as divided between an industrial and an agricultural sector and built respectively upon state enterprises and cooperatives; and upon state ownership and collective farm-cooperative ownership.<sup>567</sup> While the echoes of the collective farm compromise were latent in the 1987 State Enterprise Law's notion of the separate interest of the participant, it became explicit in the 1988 Cooperatives Law which took the cooperative form from the agrarian economy and introduced it directly into the industrial economy.

Historically, the traditional distinction between industry and agriculture determined the two basic worlds and the two legal frameworks within which the cooperatives developed in the early years of Soviet power. The agricultural cooperatives on the one hand were a legacy of the Tsarist agrarian economy. While developing during the 1920s in various forms, eventually they came to be dominated by the "collective farm" form after 1935. The industrial cooperatives on the other hand, although initially established during the years of war communism, developed most visibly during the NEP years of the early 1920s. After 1925, with the advent of state planning, they became incorporated into the state internal trade and distribution network under the auspices of Tsentrosoyuz and were eventually abolished in 1959.

**Agricultural Cooperatives** In agriculture, the cooperative movement had its roots in the peasant commune of Tsarist Russia. Attempts were made to break up this system of communal holdings following Alexander II's emancipation of the serfs in 1861 and Stolypin's decrees, enacted between 12 August and 9 November 1906.<sup>568</sup> However, on the eve of 1917 the role of the peasant and the form of the agrarian economy were still very much open questions.

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<sup>567</sup> Article 10 of the Brezhnev Constitution provided that "state (all-people's) and collective farm-cooperative ownership shall constitute the basis of the economic system of the USSR"; article 1(1) of the State Enterprise Law mentioned cooperatives as well as enterprises as "the basic link of the single national-economic complex"; and article 1(4) of the Cooperatives Law provided that "cooperative enterprises...together with state enterprises...shall be the basic link of the unified national economic complex".

<sup>568</sup> Edward Crankshaw, *In the Shadow of the Winter Palace, The Drift to Revolution 1825-1917* (Macmillan:1986), p.168, 368.



Article 105 of the 1922 RSFSR Land Code provided for three types of cooperation: joint tillage ("*tovarishchestvo c obshchestvennoi obrabotkoi zemli*") (at one extreme, the loosest form of association, under which the *dvory* operated autonomously; and carried out only principal activities, such as ploughing and harvesting, collectively); the agricultural commune ("*sel'sko-khozyaistvennaya kommuna*") (at the other extreme, where all assets were pooled and income was divided by need, regardless of contribution); and the artel ("*artel'*") (a middle form of cooperation, where only *principal assets* were pooled, and income (usually in kind) was distributed in accordance with labour contributions). The detail of each of these three forms of cooperation was set out in subordinate legislation. In addition, the code provided for the possibility of the continued application of "local customs where their application is not contrary to the law".<sup>569</sup> In practice therefore during the early 1920s a vast variety of types of agricultural cooperation existed throughout Soviet Russia, sometimes differing only by degree, and generally active in the production, marketing and distribution of produce.

While official endorsement of agricultural cooperatives can be dated to the decree of 16 August 1921,<sup>570</sup> it was the so-called "wager on the kulak" policy in the mid-1920s that signalled the beginning of the development of the agricultural cooperatives movement in a formal way. Cooperatives were then viewed as "one of the important assets for raising the level of the agricultural economy".<sup>571</sup> Although their presence was clearly a victory for the well-to-do peasant, this policy was justified in ideological terms by characterising the agricultural cooperatives as "socialist" and part of a tradition dating to Lenin,<sup>572</sup> as well as a constituting step towards the development of collective agriculture.

Following the resolutions of 14<sup>th</sup> Party Congress of April 1925 (the "Congress of Industrialisation") and the call for "socialism in one country",<sup>573</sup> official policy gradually shifted as all efforts, including the place of the agricultural cooperatives, became concentrated upon achieving the goal of rapid industrialisation of all sectors of the economy. The

<sup>569</sup> 1922 RSFSR Land Code, article 8. See also articles 55 and 77 on the application of "local customs".

<sup>570</sup> Supra n.109, p.44.

<sup>571</sup> O Sel'skokhozyaistvennoi Kooperatsii, supra n.111 (1967), p.439

<sup>572</sup> Lenin in his article "On Cooperative Societies" wrote that "under our existing regime, cooperative enterprises, as collective enterprises, differ from private-capitalist enterprises but do not differ from socialist enterprises if they are established on the land under the means of production belonging to the state and hence the working class" (45 Lenin 375). On references to cooperatives in the works of Lenin and Stalin, see Bratus' short bibliography, S.N.Bratus', *Sub'ekty Grazhdanskogo Prava* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1950), p.358. See also A.S.Tsipko, *Kak Byli Predany Zabveniyu Idei Lenina*, in *Kooperativy Sogodnya i v Budushchem* (Yuridicheskaya Literatura:1988), p.9.

<sup>573</sup> The phrase famously coined by Stalin first in his article on "The October Revolution and the Tactics of the Russian Communists" of December 1924 (6 Stalin 358).



agricultural cooperatives became gradually integrated into the state agricultural supply network, and despite some rivalry with official state organs, they played an important role in the collections of the 1926 harvest. These collections showed "that peasants were more ready to surrender their grain to cooperative rather than state organs; but it also revealed the cooperatives as becoming more and more assimilated to the role of state institutions engaged in the execution of public policy".<sup>574</sup> They were formally incorporated into the state sector in 1932.

*Collective Farms* The origin of the collective farm can also be traced to the Tsarist peasant commune, and early Soviet law treated them as cooperatives operating on the basis of one of the three forms set out in article 105 of the 1922 RSFSR Land Code.<sup>575</sup> The initial decrees and model charters suggested that the collective farm would be built on the commune form. The original charter of February 1919 noted that the "agricultural commune must serve as a sample of brotherhoodly equality of all people..." and this form was retained in the successive charters of 1922 and December 1929.<sup>576</sup>

The decree of 16 March 1927 "On the Collective Economy" was the first to stress specifically the importance of the collective farm and contemplated the development of the agrarian economy on the basis of more complex forms of cooperation.<sup>577</sup> An independent central organ, Kolkhoztentr, was set up in April 1927 and the beginning of the collectivisation movement is usually dated to this time.

The 1928 harvest was a disaster and significant state intervention was regarded as necessary to avoid the situation happening again. Active state involvement in the creation and activities of collective farms more generally began towards the end of 1928 when Kolkhoztentr launched the campaign for the establishment of large kolkhozy, which resulted in the creation of farms like the famous "Gigant" covering some 135,000 hectares. The subsequent collectivisation drive of 1929/1930 commenced with the decree of 21 June 1929 "On Measures to Strengthen the Kolkhoz System".<sup>578</sup> The particularly coercive and brutal phase lasted between October to

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<sup>574</sup> Supra n.183, p.16.

<sup>575</sup> Supra n.569. The resolution of December 30, 1926 referred explicitly to the collective farm as a type of cooperative organisation (Ob Itogakh Sovkoznogo i Kolkhoznogo Stroitel'stva, supra n.111 (1967), p.561).

<sup>576</sup> Supra n.22 (1948), pp.699-700.

<sup>577</sup> O Kollektivnykh Khozyaistvakh, supra n.111 (1967), p.590.

<sup>578</sup> O Merakh Ukrepleniya Kolkhoznoi Systemy, supra n.51, p.76.



March 1930,<sup>579</sup> and the resolution of 5 January 1930 marked the first formal intervention in the collectivisation movement by the Communist Party which offered assistance in the process of establishing collective farms.<sup>580</sup>

With the threat of a total peasant revolt, March 1930 saw a temporary respite following the publication of Stalin's article entitled "Dizzy with Success",<sup>581</sup> in which he noted that "the collective farm must not be imposed by force. That would be stupid and reactionary. The collective farm movement must operate with the active support of the main mass of the peasantry".<sup>582</sup> At about the same time, on 1 March 1930, a new model charter for the collective farm was adopted. This contemplated the use of the artel form and stressed both the voluntary principle and the combination of the personal and social interests, thereby evidencing the emerging collective farm compromise. This was reinforced by the subsequent decree of 14 March 1930.<sup>583</sup> Despite the fact that the collectivisation effort had been put on hold, the harvest of 1930 had shown the importance of the socialised sector of agriculture in the production and collection of grain; and as such the place of the collective farm as a key feature of the Stalin agrarian economy was ensured.

Due to, and during the course of the tragic history of the collectivisation effort, it seems as if the peasants had managed to extract a number of "legal concessions" from the Soviet state which had not been given to workers during the process of nationalising the industrial economy. These included the establishment of the collective farm in the artel form with the independent right of ownership; the right to participate in its management organs; the right to have a share contribution returned upon withdrawal; the right to be paid in proportion to the number of labour days worked; the right to farm a separate personal land plot; and the right to own, in a personal capacity, objects and produce associated with this personal farming.<sup>584</sup> The main features of this collective farm compromise were broadly settled by 1930, although the

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<sup>579</sup> The most significant measures were taken in January and February: "In the period of the two months (January-February 1930) the stormy growth of the collective farm movement took place: about 14 million or about 60% of all peasant economies were at that time collectivised." (supra n.120, p.43).

<sup>580</sup> O Tempe Kollektivizatsii i Merakh Pomoshchi Gosudarstva Kolkhoznomu Stroitel'stvu, supra n.51, p.153.

<sup>581</sup> 12 Stalin 191.

<sup>582</sup> Ibid p.193. As the XVI Party Congress subsequently noted: "if these mistakes had not been corrected in a timely manner by the Central Committee of the Party...this *would have threatened* a disruption of the work of the collectivisation of agriculture, to *undermine* the very *foundations* of the Soviet state - the union of the working class and the peasantry" (supra n.62, p.54). For a description of the recriminations within the Communist Party from March to June 1930, see supra n.123 (1980), pp.269-291, 311-330.

<sup>583</sup> O Bor'be s Iskrivleniyami Partlinii v Kolkhoznom Dvizhenii, supra n.51., p.194.

<sup>584</sup> Supra Sections 2.4.1 and 2.4.3.



model charter and its associated legal regime was reformed several times thereafter generally resulting in an adjustment of that compromise in favour of the state.

*Industrial Cooperatives* In the industrial economy, although the cooperative movement in Russia can be dated to the mid-1860s, its principal initial development was in the period following the 1905 revolution. Between 1906 and 1911, 5,439 cooperatives were established.<sup>585</sup> Industrial cooperatives were set up in the form of consumer, credit and production cooperatives. The consumer cooperatives were essentially elements of the internal trade and distribution network. During the period of war communism, and following the decree of 10 April 1918, they began to be absorbed in to the Soviet administration,<sup>586</sup> and came to be identifiable as instruments of state policy.<sup>587</sup> Following the decree of 16 March 1919, the consumer cooperatives were "transformed" into consumer communes. Each commune elected representatives to unions in each region that would then be represented at Tsentrosoyuz, the "single economic centre of all consumer commune unions".<sup>588</sup> In January 1920, the credit and production cooperatives were brought within this system.

Following the end of the civil war, the cooperative movement was permitted greater autonomy. First a letter from the Central Committee of the Communist Party was sent to all organisations of the party noting the importance of the cooperatives,<sup>589</sup> then, commencing on 17 May 1921<sup>590</sup> and continuing throughout 1921, a number of decrees were enacted expanding their autonomy and role in the production and distribution systems.<sup>591</sup> Gradually this autonomy was increased: all their property previously nationalised was returned and the right to engage in trade without government intervention was finally recognised. With the adoption of the 1922 RSFSR Civil Code, article 57 acknowledged that "*legally existing* cooperative

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<sup>585</sup> V. Batov, *Cooperatives in the Soviet Union* (Soviet News:1945), p.13.

<sup>586</sup> O Potrebitel'skik Kooperativnykh Organizatsiyakh, supra n.111 (1967), p.48.

<sup>587</sup> Their role was developed in a number of decrees including, the so-called "obligatory exchange" decree of 6 August 1918 which placed cooperatives on an equal status to official Soviet organs; and a decree of 21 November 1918 which nationalised internal trade and recognised the cooperative's privileged position. Others followed that gave Narkomprod the right to appoint a representative with full powers to the presidium of Tsentrosoyuz: "in the long run the effect...was to turn the cooperatives, more thoroughly and more openly than before, into accredited agents of Soviet policy" (supra n.217 (1952), p.235-6).

<sup>588</sup> O Potrebitel'skikh Kommunakh, supra n.111 (1967), p.129.

<sup>589</sup> Pis'mo TsK RKP(b) 9 Maya 1921, O Kooperatsii, supra n.111 (1967), p.226.

<sup>590</sup> O Rukovodyashchikh Ukazaniyakh Organam Vlasti v Otnoshenii Melkoi i Kustarnoi Promyshlennosti i Kustarnoi Sel'skokhozyaistvennoi Kooperatsii, ibid, p.232.

<sup>591</sup> Most importantly a decree of 7 April 1921 restored a large degree of the autonomy that they had ceded to the state during the war communism years. However, Narkomprod retained the right to require them to carry out "obligatory state tasks" (supra n.217 (1952), p.338).



organisations may possess all types of property on a level with private persons" [emphasis added]. A decree of December 1923 finally restored the voluntary principle.<sup>592</sup>

However, following the emphasis on industrialisation in the late 1920s, the industrial cooperatives like the agricultural cooperatives were again viewed as a network that could be absorbed wholesale into the state trade and distribution network. It was hoped that the cooperatives would enable the state to compete more effectively with the private sector. Industrial cooperatives after 1927 were distinguished into "independent" and "official" cooperatives. The former were characterised as organisations of the Nepmen, whereas the latter, based on small scale and artisan production, were encouraged.<sup>593</sup> From 1927 the state (through syndicates and *torgi*) and industrial cooperatives gradually took over from private trading. By the early 1930s, "legally existing cooperatives" within the meaning of article 57 of the 1922 RSFSR Civil Code were only those that existed within the official state cooperative network. Thus Gsovski concluded "co-operatives are in fact completely controlled by the government but differ from governmental enterprises in that those who work in them have shares but are paid only for contribution in labor".<sup>594</sup> The importance of the cooperative system in the industrial economy increasingly became marginalised with the development of the Soviet economy through the late 1950s. Eventually they were abolished entirely by Khrushchev in his early attempts to reform the Stalin economy.<sup>595</sup>

The cooperatives, and in particular collective farms, therefore represented a traditional economic organisation within the national Soviet economy. As has been noted, the Brezhnev Constitution referred to cooperatives in article 7 noting that they were a type of "social organisation", and article 10 went on to provide for "collective farm-cooperative ownership" as a form of socialist ownership.<sup>596</sup> In view of the fact that there was a separate form of ownership for the cooperatives, the list of juridical persons in article 11 of the 1961 FPCivL distinguished specifically "the collective farms, intercollective and other co-operative organisations and their associations" from other juridical persons.<sup>597</sup>

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<sup>592</sup> O Reorganizatsii Potrebitel'skoi Kooperatsii na Nachalakh Dobrovol'nogo Chlenstva, supra n.111 (1967), p.385.

<sup>593</sup> O Kustarno-Remeslennoi Promyshlennosti i Promyslovoi Kooperatsii, supra n.111 (1967), p.639.

<sup>594</sup> Supra n.22 (1948), p.413.

<sup>595</sup> Supra n.137, p.312.

<sup>596</sup> This was elaborated both in the 1961 FPCivL (article 23) and the various provisions of the civil codes. See supra Section 2.3.2 and infra Section 6.4.4.2.

<sup>597</sup> Supra Section 2.5.



In the early 1980s, the collective farm was the principal form of cooperative.<sup>598</sup> However, the Soviet legal system still recognised a number of other cooperative forms which operated in discrete areas of the economy.<sup>599</sup> The formal resurrection of the cooperative form in the Soviet *industrial* economy during *perestroika* began gradually with the adoption of a number of decrees culminating in 1988 with the enactment of Cooperatives Law. Following the decree of 9 January 1986 "On Measures for the Further Development of Consumer Cooperatives",<sup>600</sup> the broadening of the cooperative sector of the industrial economy developed through the lengthy decree of July "On the Perfecting of Planning, Economic Stimulation and Management in State Trade and Consumer Cooperatives",<sup>601</sup> and the decree on the organisation of state procurement and processing of secondary raw materials on a cooperative basis (attaching a model charter).<sup>602</sup>

During 1987, new model charters were adopted for cooperatives for public catering; for service establishments of the populace; for the production of goods of national needs and for the manufacture of confectionery and pastries.<sup>603</sup> These were all broadly similar in detail. The last decree of 1987 relating to cooperatives introduced a set of general measures aimed at improving the organisation of the sale of goods produced by cooperatives and citizens conducting individual labour activity.<sup>604</sup> The cooperative movement developed throughout the latter half of 1987 on the basis of these decrees. By late November there were 700 registered

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<sup>598</sup> By 1982 there were 25,800 collective farms in the Soviet Union composed for more than 13.3 million people (supra n.93, p.43).

<sup>599</sup> Seven types were traditionally distinguished comprising: the collective farm; the fishing collective farm and their unions; the artel of gold prospectors; consumer cooperatives and their unions; intereconomic organisations (intercollective farm and other intercollective farm organisations); cooperatives for the construction and exploitation of objects of consumer designation (multi-apartment housing blocks, dachas, garages etc); and horticultural partnerships (supra n.41 (1986), p.149 *et seq*).

<sup>600</sup> O Merakh po Dal'neishemu Razvitiyu Potrebitel'skoi Kooperatsii, *Postanovleniya* (January 1986), no.40, p.109.

<sup>601</sup> O Sovershenstvovanii Planirovaniya, Ekonomicheskogo Stimulirovaniya i Upravleniya v Gosudarstvennoi Torgovle i Potrebitel'skoi Kooperatsii, *Postanovleniya* (July 1986), no.842, p.155.

<sup>602</sup> Ob Organizatsii Zagotovki i Pererabotki Vtorichnogo Syr'ya na Kooperativnoi Osnove, *Postanovleniya* (August 1986), no.988, p.201.

<sup>603</sup> O Sozdanii Kooperativov Obshchestvennogo Pitaniya, *Postanovleniya* (February 1987), no.160, p.89; O Sozdanii Kooperativov po Bytovomu Obsluzhivaniyu Naseleniya, *Postanovleniya* (February 1987), no.161, p.100; O Sozdanii Kooperativov po Porizvodstvu Tovarov Narodnogo Potrebleniya, *Postanovleniya* (February 1987), no.162, p.112; and O Sozdanii Kooperativov po Vyrabotke Konditerskikh i Khlebobulochnykh Izdelii, *Postanovleniya* (August 1987), no.1042, p.93.

<sup>604</sup> O Merakh po Uluchsheniyu Organizatsii Prodazhi Tovorov Proizvodimyykh Kooperativami i Grazhdanami, Zanimayushchimiya Individual'noi Trudovoi Deyatel'nost'yu, *Postanovleniya* (September 1987), no.1097, p.382.



in Moscow alone and Leonid Abalkin, director of the Institute of Economics, predicted that they would account for between 10-12% of the national income within the next 10 years.<sup>605</sup>

An unpublished decree of March 1988 indicated that a new law on cooperatives was nearing completion, and directed work on the draft to be finished by 1st May.<sup>606</sup> The Cooperatives Law was finally adopted on 26 May 1988 and was amended several times, principally in June 1990 (the "**June 1990 Amendments**").<sup>607</sup> The Cooperatives Law set out general principles, as well as specific rules, relating to collective farms and agricultural cooperatives, production cooperatives, and consumer cooperatives and societies including cooperative banks.<sup>608</sup> It had a number of general similarities with the State Enterprise Law. First, like the State Enterprise Law, it was a "law" (and not a decree or statute) and this suggested that cooperatives were to be a central plank in the development of the new industrial socialist economy. Furthermore, like the State Enterprise Law, it was exceedingly long (running to some 54 articles, each with generally at least 4 sub-articles). Finally, in the same way that the State Enterprise Law had unified the legal regime of previously two distinct organisations (enterprises and associations), so the Cooperatives Law unified what previously had been two distinct areas of law (collective farm law and the law on industrial cooperative organisations) thereby providing for a single legal organisational structure.<sup>609</sup> It was the first time in the later Soviet period that organisational forms from the industrial and agricultural sphere had been so directly married under the same basic legislation.

The use of the cooperative was yet another attempt to reform the framework and function of an established form of Soviet organisation (i.e. the collective farm) with the aim of tackling the structural problems at the heart of the industrial command economy, and to "further perfect" the operation of that economy.<sup>610</sup> While the 1987 state enterprises were developed

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<sup>605</sup> Supra n.547, p.59.

<sup>606</sup> O Poryadke Obobshcheniya Zamechanii i Predlozhenii Trudovykh Kollektivov i Grazhdan po Proekty Zakona SSSR "O Kooperatsii v SSSR" i Dorabotke ego s Uchetom Vse-Narodnogo Obsuzheniya, *Postanovleniya* (March 1988), no.300, p.14.

<sup>607</sup> O Vnesenii Izmenenii i Dopolnenii v Zakon SSSR "O Kooperatsii v SSSR", *Vedomosti SND SSSR* (1990), no.26, item 489.

<sup>608</sup> These distinctions were clearly indebted to the NEP era cooperatives which distinguished agricultural cooperatives, production cooperatives, credit cooperatives and consumer cooperatives.

<sup>609</sup> The "cooperative" governed by the general provisions of the Cooperatives Law was now to be used "in agriculture, in industry, construction, for transport, in trade and public catering, in the sphere of paid services, and other branches of production and socio-cultural life." (Cooperatives Law, preamble, article 3(1)).

<sup>610</sup> Article 1(1) of the Cooperatives Law assumed cooperatives would be able to give a "new impulse" to the development of various spheres of economic life, including: "to uncover the great potential possibilities of cooperative societies and the growth of their role in the acceleration of the social-economic



from an existing organisational form within the industrial economy (the state enterprise), the 1988 cooperatives by contrast were developed upon an organisational form that until then had developed primarily from within the agrarian economy, namely the collective farm. As has been shown, the characteristics of the collective farm, and the agricultural economic settlement following the 1930s collectivisation drive were very different from those of state enterprises and the industrial economic settlement. The Cooperatives Law seemed to be enacted upon the premise that the previously agrarian framework of the collective farm could be translated into the industrial sphere with slight alteration to the balance between social and personal interests, and without prejudicing the socialist foundations of the industrial economy thereby preserving the state's overall control of, and ability to plan, the national economy.

Like the state enterprises,<sup>611</sup> the cooperatives were declared to be "socialist",<sup>612</sup> and were expressed to be founded upon "Leninist ideas on cooperative societies as applied to the modern stage of the construction of socialism in the USSR".<sup>613</sup> As with all the expressions of the participation model, the Cooperatives Law was not intended to undermine the concept of a planned economy *per se* or existing forms of ownership, but instead sought to "restructure" the economy by incorporating the twin pillars of incentivisation and limited democracy.<sup>614</sup> It is perhaps for this reason that the 1988 cooperatives were explicitly referred to as enterprises, or strictly speaking as "cooperative *enterprises* (organisations)".<sup>615</sup> The "enterprise" was

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development of the country, to strengthen the process of democratisation of economic life ...and create conditions for involving the broad population in cooperatives" (preamble); the "saturating of the market with high quality goods and services, making them cheaper, and satisfying more fully the material and spiritual needs of the Soviet people" (article 1(2)); satisfying the "economic and social development of society [and], the rational use of material and labour resources"(article 1(3)); "raising the efficiency of economic operations...[and ensuring] higher labour productivity...to facilitate increased efficiency of economic operations in every way" (article 1(5)); and the "satisfaction of the needs of the national economy and population for foodstuffs, consumer goods [and] housing...enhanced efficiency, improvement of the quality of productions...and growth of labour productivity...and wasteless and resource-saving technologies shall be worked out and introduced" (article 4(1)).

<sup>611</sup> Supra n.566.

<sup>612</sup> Cooperatives Law, articles 1(1) and 2(2) actually called these cooperatives "the *socialist* cooperative society" [emphasis added]. See for other references to "socialism" in the Cooperatives Law: article 10(1) ("socialist legality"), articles 6(1) and 14(1) ("socialist self-management"), and article 17(1) ("socialist economic operations").

<sup>613</sup> Cooperatives Law, preamble. On Lenin's ideas on cooperatives see supra n.572.

<sup>614</sup> As Batygin noted of the Cooperatives Law, "from all the measures of the social-economic polity adopted by the party for the purpose of renewing socialism, the law on cooperatives has the most important political and practical significance" (G.S.Batygin, *Pochemu Kooperator v Nemilosti*, in supra n.572 (1988), p.50).

<sup>615</sup> Cooperatives Law, articles 1(1) and 1(4) [emphasis added].



traditionally the Soviet judicial person developed on the basis of the Stalin forms of ownership regime to operate within the planned industrial economy.<sup>616</sup>

It shall be argued that the 1988 cooperative enterprises fell within the participation model and radicalised the steps taken by the 1987 legislation on state enterprises. Most importantly, unlike state enterprises, the state was not the legal owner of the cooperatives in any necessary respect.<sup>617</sup> Furthermore, unlike state enterprises, the cooperatives had the independent right (and an independent form) of ownership separate from that of the state, characterised as "collective farm-cooperative ownership". This type of separation from the state was something that had not even been envisaged in the contract-based concession model, where the state generally retained in part the role of creator owner (through its ownership of the Soviet participant) and continued to act as direct owner of the property contributed to the joint enterprises by the Soviet participant.<sup>618</sup> This cleaner separation from the state in the second expression of the participation model further exacerbated the possibility for the development of "independent" interests in the Soviet economy that may not have been coincident with those of the state.<sup>619</sup>

The effect was therefore to deepen the fragmentation of the unitary all-people's state marked by the divisions latent in the 1987 state enterprises legislation; and in addition, to accelerate the dismantling of the core of the governance system of the confirmation model. In this second expression of the participation model the state was no longer the creator-owner, nor the property-owner, and hence its role as economic sovereign became questioned. However, despite the loss of direct ownership of a certain portion of the domestic economy, the Soviet state leveraged upon its position as legal sovereign to preserve its "administrative rights" through specific mandatory provisions of the Cooperative Law relating to the operation of cooperatives within the national economy (in much the same way that the Soviet state continued to control the collective farms and, to some extent, joint enterprises).<sup>620</sup> It was only in the final expression of the participation model, in the form of the leased enterprise, that

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<sup>616</sup> On the meaning of "the enterprise", supra Section 5.5 and infra Sections 7.5 and 7.6.

<sup>617</sup> On the question of the identity of the owner of the cooperative, infra Section 6.4.1.

<sup>618</sup> Supra Section 5.4.2.

<sup>619</sup> This had always been somewhat implicit within the cooperative form: "Cooperative organisations differ from other social organisations in that they are created for the effectuation of economic activities in the interests of *their members*" (*Sovetskoe Grazhdanskoe Pravo* (Yuridicheskaya Literatura:1983), p.67 [emphasis added]). As such, the state specifically governed their activities by characterising them as part of the unified planned economic network (see supra Section 2.4.1).

<sup>620</sup> "The Soviet state, effectuating general leadership over the activities of the cooperative, coordinates it in the procedure as set out in the plan..." (supra n.41 54, p.311). See infra Section 6.4.4 and supra Section 5.2.



those administrative relationships themselves were directly undermined by an organisational form founded explicitly upon the civil law of contract.

#### 6.1.4 *1989 Leased Enterprises*

References to the concept of the lease, and the possibility for "transforming" one type of enterprise into a leased enterprise, appeared not only in the State Enterprise Law,<sup>621</sup> but also in the Cooperatives Law.<sup>622</sup> These provided the first hints of the possibility of using the lease as a mechanism by which a collective (namely a cooperative or other form) might be permitted to lease assets from an enterprise or perhaps even an entire enterprise itself from the state.

While the first two expressions of the participation model were built upon existing organisations within the Soviet economy, the third expression looked not to an existing organisation, but to an existing form of contract, the lease. The origins of this contract and its use in the context of the law on industrial organisations once again can be traced to the 1920s.

Unfortunately the Soviet law on "lease" was plagued with a plethora of terminology, the precise meaning of which was often quite difficult to identify. Two basic terms were used: the "lease" ("*arenda*"), and the "contract for property hire" ("*imushchestvennyi naem*"). The term "lease" was traditionally used in the context of land law and was specifically mentioned in the 1922 RSFSR Land Code. Primary *civil law* legislation omitted any reference to the term "lease" and only referred to the "contract for property hire". The contract for property hire had been a feature of pre-revolutionary Russian law,<sup>623</sup> continued to be referred to in the 1922 RSFSR Civil Code,<sup>624</sup> and remained as a distinct form of contract in the framework of the 1961 FPCivL<sup>625</sup> and the 1960s civil codes.

One of the earliest references to the legal mechanism of the lease was to the lease of enterprises in the Decree of 28 June 1918 on nationalising key sectors of industry. During this time of civil war, while it was always possible to undertake formal "nationalisation" through legislative diktat, implementation in practice was of course going to be problematic and gradual. The decree of June 1918 carefully avoided an immediate and abrupt alteration of management structures by providing that although the relevant enterprises were to be

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<sup>621</sup>       Infra n.710.

<sup>622</sup>       For example, Cooperatives Law articles 5(1), 5(4), 8(3), and 27(4). Article 29(3) of the Cooperatives Law was the first place to mention all three participation enterprises in the same article.

<sup>623</sup>       Supra n.88, p.355.

<sup>624</sup>       Article 152 *et seq.*

<sup>625</sup>       Article 53 *et seq.*



nationalised (ie ownership thereof passing to the state), until Vesenkha adopted specific decrees for specific enterprises, the existing management would continue to have the right to operate the enterprise which "shall be deemed to be in rent free leased use".<sup>626</sup> As such, from the very early days of Soviet power, the lease was used as a mechanism by which the Soviet legal system preserved state ownership of an asset while at the same time providing the legal basis for continued operational control by others.

The NEP period saw the development of the use of the lease in the context of the "private" economy in two principal contexts: the lease of an enterprise and the lease of land. The basis for the lease of enterprises generally was contained in a dekret of Sovnarkom of 5 July 1921.<sup>627</sup> This dekret was considered to have been promulgated pursuant to article 153 of the 1922 RSFSR Civil Code, despite the fact that that article used the term "hire" rather than "lease". Article 1 of the dekret stated that "the right to lease state industrial enterprises with the purpose of their exploitation shall be granted to cooperatives, partnerships and other associations." This was developed in 1923 Trusts Dekret where article 28(a) contemplated the leasing of a part of a trust pursuant to the provisions of the 1922 RSFSR Civil Code. (Again, while the 1923 Trusts Dekret used the term "lease", the civil code only used the word "hire"). In this way the term "lease" gradually came to be used in subordinate legislation interchangeably with the term "contract for property hire".<sup>628</sup>

The lease of land developed during the mid-1920s as the state put its "wager on the kulak". Unlike primary civil law legislation, the 1922 RSFSR Land Code did specifically refer to the "lease contract" and formally contemplated the leasing of land in restricted instances. Subordinate legislation of this period also referred to the lease as a mechanism for transferring property rights, in particular relating to land plots and the subsoil. During NEP, article 28 of the 1922 RSFSR Land Code was amended to allow households the right to lease all or part of their land if they had been "temporarily weakened as a consequence of some natural disaster (bad harvest, fire, cattle disease etc) or [in the event of] an insufficient inventory or labour

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<sup>626</sup> Supra n.111 (1967), p.95 (article III).

<sup>627</sup> O Poryadke Sdachi v Arendu Predpriyatii, Podvedomstvennykh Vyshemu Sovetu Narodnogo Khozyaistva, *SU* (1921), no.53, item 313. This very early concept of leasing "an enterprise" evidenced the basic assumption under Soviet law that an enterprise could be viewed as an indivisible object of the law on ownership.

<sup>628</sup> See use of the term "lease" in the commentary to articles 152 and 153 of the 1922 RSFSR Civil Code and in the subordinate legislation noted supra n.182 (1928), pp.508-532. A legal encyclopedia of that period under the definition of property hire contract stated "see Lease" (*Entsiklopediya Gosudarstva i Prava*, Vyp.4 (Izdatel'stvo Kommunisticheskoi Akademii:1926), p.1066).



force".<sup>629</sup> This amendment therefore provided a further opportunity to lease land "under the guise of a concession to temporary emergencies".<sup>630</sup>

Leasing in the private economy only began to be curtailed following the failure of the harvest of 1925 which signalled a reversal of policy as the emphasis moved from agriculture to industry. Following the 14<sup>th</sup> Congress of Industrialisation in 1925 and the increase in the role of central planning, the lease of land came to be presented as a feature of capitalist societies,<sup>631</sup> and the lease of enterprises became less attractive in light of state policy aimed at increasing direct control over the economy. During 1927 a number of measures were adopted that restricted the periods and conditions for the lease of land,<sup>632</sup> and in 1928 the Supreme Court of the RSFSR even decided to permit applications for the termination of leases of state enterprises where the leased enterprise did not contribute to the industrial efforts of the USSR or where its productivity had been reduced.<sup>633</sup> An explicit prohibition on the leasing of agricultural land was finally introduced in 1937,<sup>634</sup> and the 1968 FPLand and the subsequent land codes removed all references to the lease as a method of landholding (adopting instead the concept of "land use" as the mechanism by which land was allocated by the state).<sup>635</sup>

While the "lease" of land and enterprises effectively came to an end during the 1930s, the use of the term "lease", as distinct from "property hire", did survive in *subordinate* legislation of the later Soviet period including the Enterprise Statute,<sup>636</sup> and usually was applied in the

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<sup>629</sup> Supra n.17, p.317.

<sup>630</sup> E.H.Carr, *Socialism in One Country 1924-1926, Volume One* (1958, reprinted Macmillan:1978), p.257.

<sup>631</sup> See, for example, *Zemel'noe Pravo* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1958), pp.291-297, and B.V. Erofeev, *Sovetskoe Zemel'noe Pravo* (Izdatel'stvo Vyshaya Shkola:1965), pp.314-318.

<sup>632</sup> Supra n.183, p.134.

<sup>633</sup> Case No 32471-1928, *Sudebnaya Praktika* (1928), no.24, p.3.

<sup>634</sup> Supra n.22 (1948), p.706.

<sup>635</sup> See, generally, *Zemel'nye Pravootnosheniya v SSSR* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1958), p.127 *et seq.*, and *Sovetskoe Zemel'noe Pravo* (Izdatel'stvo Yuridicheskaya Literatura:1981), p.145 *et seq.*

<sup>636</sup> Article 16 of the Enterprise Statute provided for the right of a state enterprise to lease buildings and equipment that it was not using to other enterprises and organisations at centrally established lease payments. A commentary to that article (again noting the interchangeability of the terminology) explained that "these relationships are regulated by the contract of property hire (lease) in the procedure and on the conditions provided by articles 275-278 of the RSFSR CC and corresponding articles of the civil codes of the other union republics..." (supra n.245, pp.50-51). For other examples of subordinate legislation of the later Soviet period using the concept of "lease", see supra n.244, p.321 and p.329.



context of immoveables. In such instances, provisions relating to lease were considered to be regulated by the provisions of the civil codes relating to "the contract for property hire".<sup>637</sup>

The FPLease adopted in 1989 can therefore be seen as an extension of the existing law of property hire as set out in the 1961 FPCivL and civil codes and other subordinate legislation on lease. By explicitly using the term lease, *arenda*, it placed this new initiative firmly within the NEP era legislation, and incorporated the lease within primary civil law legislation for the first time in Soviet history. The "leased enterprise" itself, like the other participation enterprises, was formed from within the mainstream of Soviet law, but was indebted to the radical form of lease structure as applied during the NEP years.

Similar to the cooperatives legislation of 1986-1988, the introduction of the legislation on lease was gradual. Although the use and importance of the lease was hinted at in the State Enterprise Law and the Cooperatives Law, the first decree of this period to contemplate explicitly the use of the lease in relation to land and enterprises was the USSR Supreme Soviet decree "On Lease and Lease Relations in the USSR" passed on 7 April 1989.<sup>638</sup> The FPLease was then adopted on 25 November 1989, and shortly afterwards on 20 March 1990 a decree "On the Procedure for Leasing Enterprises (Associations) of Union Subordination their Property" was passed. This decree excluded defence, communications, transport, oil-energy and other specific sectors from the ambit of the FPLease.<sup>639</sup>

The basic elements of the participation model were identifiable in the preamble to the April 1989 decree which predated the FPLease. The decree aimed at "...protecting the rights of lessors, strengthening their interestedness and responsibility in the attainment of the highest final results of labour"; and like the 1987 state enterprise and 1988 cooperatives, the lease was

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<sup>637</sup> In common with past practices, primary civil law legislation (eg the 1961 FPCivL (article 56 *et seq*) and the civil codes (eg RSFSR CC, article 295 *et seq*) only used the word hire ("*naem*"), and not lease, in the context of (the hire of) dwelling premises. A textbook written in 1983 however noted their interchangeability referring to: "The contract for property hire (sometimes called by the terms contract of lease or rent of property)..." (supra n.619, p.237. This question of terminology prevails to date: one civil law textbook of the current post-Soviet period noted "Today's current Civil Code considers the lease and the property hire as interchangeable" and speculated that the origin of the distinction might be traceable to French law (which distinguishes the hire of moveable property from the lease of immovable property) and German law (which makes a similar distinction) (*Grazhdanskoe Pravo, Uchebnik Chast' 2* (Prospect:1997), p.151, footnote 1). Other terms in Russian have been used in the Soviet legal system for contracts granting the right of use of an asset (for example, "*prokat*" (to rent)), but these are not significant for present purposes.

<sup>638</sup> Ob Arende i Arendykh Otnosheniyakh v SSSR, *Vedomosti SSSR* (1989), no.15, item 105.

<sup>639</sup> O Poryadke Sdachi Predpriyatii (Ob'edinenii) Soyuznogo Podchineniya i ikh Imushchestva v Arendu, *Postanovleniya* (March 1990), no.280, p.88.



again conceived as a socialist measure that was to be used in order to make the economy more responsive, while preserving in general the existing Soviet planned economy. The preamble to this decree described the lease as "a new progressive form of socialist economy" to be used in the quest for "greater effective industrial and agricultural production" through activating the human factor and creating an interest of the participant in the outcome of his labours.

The FPLease, adopted following the April decree, was the briefest of all the legislation within the participation model, spanning a mere 33 articles, with only 12 devoted specifically to the leased enterprise. This was probably because the FPLease (unlike the State Enterprise Law and the Cooperatives Law) was adopted in the form of "fundamental principles", and as such was only intended to set out a basic framework upon which more detailed legislation in the form of republic codes on lease could have been adopted (no such codes were in fact ever adopted).

As was illustrated by the early decree of 28 June 1918,<sup>640</sup> the innovation of the lease was that it presented the opportunity of preserving formal state ownership of an asset, while transferring to another, control and the right to profits for a negotiated period of time. It was an attempt to provide the economic incidents of ownership without affecting the formal legal position. Like the NEP era legislation, leasing was available in relation to a specified list of objects including land,<sup>641</sup> as well as "enterprises (associations), organisations, structural entities of associations, production entities, shops, other subdivisions of enterprises";<sup>642</sup> and it was the lease of the latter which gave rise to the so-called "leased enterprise" ("*arendnoe predpriyatie*").

The importance of the 1989 leased enterprise was not only that it built upon the concept of separate interests, and that it consolidated the dismantling of the governance regime of the confirmation model achieved by the earlier expressions of the participation model, but also that it firmly (but only implicitly) reorientated the juridical person back into the world of "contract" from the world of "forms of ownership". The leased enterprises were born of a tradition that can be traced both to the NEP legislation on leasing, and to the existing bridge, the contract for joint activity, that was the grandfather of all contract-based associations. As relations therefore moved back to the realm of civil law, the balance, embodied by democratic centralism and the collective farm compromise, tilted firmly towards the arena of the market

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<sup>640</sup> Supra n.626.

<sup>641</sup> Indeed, the subsequent 1990 FPLand, like the former 1922 RSFSR Land Code, provided again for the lease as one of the three methods for holding land: (in addition to possession and use) (articles 5, 6, 7).

<sup>642</sup> FPLease, article 3.



where participants' interests were defined autonomously, where organisations were "owned" by participants, and where the state's rights, as quasi-feudal overlord, to "administer" the economy through instruction were increasingly curtailed.

## 6.2 The Three Expressions of the Participation Model

The argument that the 1987 state enterprises, 1988 cooperative enterprises and 1989 leased enterprises formed different expressions of a single unifying model or policy is one that may on its face seem unlikely. Indeed the link between these three organisations is rarely, if ever, made in commentaries and textbooks. In addition, the connection between all these enterprises and the contract for joint activity and collective farm legislation has, to the knowledge of the author, never been characterised or understood in the terms presented by the participation model, despite the fact that most evidently the Cooperatives Law directly regulated the operation of collective farms as well as industrial cooperatives. In the literature that preceded the 1990 Law on Enterprises, these three enterprises were typically regarded as discrete separate initiatives;<sup>643</sup> and in the literature written after the adoption of the 1990 Law on Enterprises and 1990 Ownership Law, although state enterprises, cooperatives and leased enterprises were all seen as "enterprises" (almost by definition in accordance with the new law), no attempt was made to analyse their similarities with a view to developing an overarching theoretical understanding of their structures.<sup>644</sup>

It is argued in this Chapter that each of the 1987 state enterprises, 1988 cooperative enterprises and 1989 leased enterprises were in fact different expressions of a single model where the Soviet state in slightly different ways explored the possibility of creating organisations based on the notion of active "participation". It was therefore no coincidence that they all were called "enterprises".<sup>645</sup> All these enterprises adopted slightly different levels of the right to participate through the democratic process coupled with economic

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<sup>643</sup> For example, the Soviet state publisher of legal books, "Yuridicheskaya Literatura", published in a single book the set of 1987 decrees relating to the reform of the state enterprises (supra n.552); published another separate book on the role and function of these new 1987 state enterprises (*Predpriyatiye - Zakon - Upravlenie* (Yuridicheskaya Literatura:1989)); and published a third separate book on the role and function of the cooperatives, including relevant legislation (supra n.572 (1988)). Finally a separate book on leasing was published after the collapse of the Soviet Union (S.A. Gerasimenko, *Arenda Kak Organizatsionno-Pravovaya Forma Predprimatel'stva* (Izatelstvo BEK:1992)). None of these studies made more than a passing reference to the other enterprises. This was generally reflected in the treatment in western literature (see for example Philip Hanson, *From Stagnation to Catastroika - Commentaries on the Soviet Economy, 1983-1991* (Praeger Publishers:1992), chapter 10 (The Enterprise Law and the Reform Process), and chapter 12 (The Draft Law on Cooperatives: An Assessment)).

<sup>644</sup> On the significance of the 1990 Law on Enterprises in the development of the industrial organisations, see infra Section 7.5.

<sup>645</sup> See supra n.616.



incentivisation and the legacy of coercive law. However, although they all provided the opportunity for participation, they were never intended to be, in the words of Ioffe and Maggs, "a change of the system itself". It gradually became clear that a system based on an "all people's state" with unlimited political and economic state power could not co-exist with the recognition of interests separate from that state - and the development of such interests was started by the logic of the 1987 reform of the state enterprise and continued through to the 1989 leased enterprises.

### 6.3 1987 State Enterprises - Separating the Private from the Public

#### 6.3.1 *The State Enterprise and the Labour Collective*

The 1987 state enterprises were the first expression of the participation model within the Soviet economy. As has already been noted, reforming the state enterprise as a starting point for the *perestroika* of industrial organisations was perhaps an obvious choice. The law governing their regulation dated to the 1965 Enterprise Statute, and there had been a "tradition" since the 1920s of periodically re-examining the legal framework of the state enterprise in line with changing macro-economic policies, stressing alternatively centralisation and then decentralisation.<sup>646</sup>

In a market economy, the operation of that economy coupled with mandatory corporate law rules provide certain systemic incentives to align the interests of the shareholders, directors and workers. Ownership provides the necessary incentive to ensure effective monitoring of operations and the activities of directors generally, as ownership carries with it the right to vote on the appointment of the executive organ (ie directors), to receive profits in the form of dividends, and to benefit from an increase in the value of ownership interests (eg shares) through the equity market. Structural constraints of corporate law are devised in part to ensure that, where there may be a risk of abuse, interests of the owners and the directors are realigned, and interests of minorities are protected.<sup>647</sup> Finally, Smithian hidden hand theory suggests that the cumulation of all companies and interest groups working in their narrow self-interest in the market place actually has the net effect of producing the most efficiencies for the market as a whole.

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<sup>646</sup> See supra n.221.

<sup>647</sup> The corporate law theory beneath this summary can be traced to Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* (1968, reprinted Transaction Publishers:1991) and Coarse's article on The Nature of the Firm in 1937 (see R.H.Coarse, *The Firm, the Market and the Law* (The University of Chicago Press:1988)).



The Soviet system as characterised by the confirmation model was radically different and was more akin to a feudal settlement than a market economy. The state had the right of absolute ownership and control over the whole economy (through its roles as creator-owner, property-owner, appointer of the one-man manager, and economic and legal sovereign). In practice, this command economy did not systemically incentivise the individual worker who was deprived by the ubiquitous dictatorial institutions of the Communist Party and state of the usual means of representation and protest, including trade unions and parties. Therefore, bereft of collective institutions that may have represented the workers' interests in the narrow sense, workers generally exercised the only avenue for dissent that the system allowed - the withdrawal of their labour.<sup>648</sup> An open admission of the existence of an "interest of the worker" as separate from that of the state would have been problematic in the context of Soviet ideology, the logic of the planned economy, and the theory of the all-people's state. Yet, without some mechanism for incentivisation, it seemed that the worker would be systemically encouraged to withhold his labour. Bonus payments and labour discipline were the traditional incentivisation methods used,<sup>649</sup> and therefore an "interest" of the worker separate from that of the state was always implicit within Soviet wage payment and labour law.

This systemic incentivisation problem was unmasked and explicitly acknowledged by Gorbachev. Probably, without an understanding of the practical and ultimate consequences of such an acknowledgement,<sup>650</sup> "a new organisation" was introduced on the basis of stressing the central role of the participant, the individual worker, and elaborating a regime for incentivising his interest. In short, the aim was to develop in each worker "a deep personal interestedness in the economic use of all-people's ownership, [and] his organic participation in the affairs of the collective and the state,"<sup>651</sup> thereby realising in practice the view of Venediktov and Bratus who had conceived of the labour collective as the "heartbeat" of the state enterprise.<sup>652</sup>

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<sup>648</sup> This argument is developed by Filtzer (see Donald Filtzer, *Soviet Workers and the Collapse of Perestroika - The Soviet labour process and Gorbachev's reforms, 1985-1991* (Cambridge University Press:1994)).

<sup>649</sup> See *infra* Section 6.3.2.

<sup>650</sup> The consequences of the participation model for the theory of the all-people's state and state control of a single national economic complex are evaluated throughout this Chapter. They resulted in the fundamental reforms of spring 1990 which are outlined and assessed in the next Chapter.

<sup>651</sup> State Enterprise Law, article 1(3).

<sup>652</sup> *Supra* n.57 (1948), pp.664-673; and *supra* n.572, pp.104-115. Indeed this was partly reflected in the drafting of 1965 Enterprise Statute.



Despite agreement on the general incentivisation function of this new organisation, the detail of how to achieve the resurrection of the interest of the participant in practice, without prejudicing the state's overall control of the economy, was not something that had been previously worked out. The State Enterprise Law was the first attempt to do so in the *perestroika* period.

Most of the techniques adopted by the State Enterprise Law can be traced to the law of collective farms. A certain amount of confusion however inevitably resulted when the collective farm compromise was transported and translated into the industrial economy, and applied to an organisation which, in contrast to the collective farms, had traditionally been wholly owned by the state.

The collective farm represented a balance between the interests of the state (ie the "social interest") and the interests of the collective farmers and their households (ie the "personal interest");<sup>653</sup> and in 1987 the new state enterprise was also "opened up" to interests other than those of the state, seemingly in the pursuit of a similar dynamic. However, unlike the collective farm, there had not previously been any tradition of distinguishing different interests within this industrial organisation and hence the confirmation model only provided for a regime of one owner and a one-man manager. In a break from the past, the State Enterprise Law formally recognised (among others) the interests of: the state and Soviet society generally (ie the formal owners), those of the labour collective and its members (ie the participants/economic owners), and those of the enterprise itself.

The State Enterprise Law in many places anthropomorphised the concept of "the enterprise" by providing that "the enterprise" had certain rights and obligations.<sup>654</sup> In the context of a new model that contemplated competing interests within the organisational forum, it was not exactly clear in whose interests "the enterprise" was intended to act.<sup>655</sup>

In some places the State Enterprise Law assumed that the interests of the labour collective *were* the interests of the enterprise and could not be distinguished. The clearest expression of the labour collective "as the enterprise" was in article 2(3) where the labour collective was

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<sup>653</sup> On the collective farm compromise, see *supra* Sections 2.4.1 and 6.1.3.

<sup>654</sup> See generally *infra* Sections 6.3.4.1 and 6.3.4.3.

<sup>655</sup> In the confirmation regime this was less problematic as the rights "of the enterprise" could only have been construed as rights of the one-man manager acting on behalf of the enterprise in furthering the interests of the all-people's state.



described as the "fully fledged proprietor ("*khozyain*")<sup>656</sup> of the enterprise [which] shall autonomously decide all questions of production and social development." This was reflected again in article 1(2) which referred to the labour collective as having the right to use "all-people's ownership" (ie the enterprise) as "proprietor".

At other places however, the State Enterprise Law assumed that the interests of the enterprise and the labour collective *could* be distinguished although for present purposes were coincident.<sup>657</sup> At other times still, the interests were distinguished and assumed not to be coincident. For example, articles 3(5) and 4(4) both referred to the right of the "the enterprise...with the consent of the labour collective...". Article 8(2) went even further and provided that "the enterprise shall form a stable labour collective", thereby suggesting that it was the enterprise that was the proprietor of the labour collective and not the other way around.

Perhaps the best understanding of the concept of "the rights of the enterprise" is by reference to the traditional view of identifying rights "of a juridical person" with the rights of its executive body. In the case of the 1987 state enterprise, the executive body was the one-man manager. Indeed, the State Enterprise Law directly referred to the one-man manager as acting "on behalf of the enterprise".<sup>658</sup> Unlike the one-man manager of the confirmation model, the one-man manager of the participation model should be understood as an executive body required to act in the combined interests of the state *and* the participant (ie the labour collective) and not just in the interests of the state alone.<sup>659</sup>

Therefore, like the collective farm compromise that balanced the interests of the state with those of the *dvor* and the collective farm members, the State Enterprise Law elevated the role of the labour collective to that of a "participant" with separately identifiable interests and accordingly referred throughout to a balance or combination of interests with those of the state.<sup>660</sup> As a result, the 1987 state enterprise fell clearly outside the traditional confirmation

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<sup>656</sup> The Russian word "*khozyain*" suggested therefore that the labour collective had control over the economic operations of the state enterprise but avoided the ideologically sensitive term "*sobstvennik*" (owner).

<sup>657</sup> For example, State Enterprise Law, article 2(3) stated "achievements and losses in the work *of the enterprise* [NB not the work of the labour collective] shall directly effect the level of *khozraschet* revenue *of the collective*, the well-being of each worker" [emphasis added].

<sup>658</sup> State Enterprise Law, article 6(4).

<sup>659</sup> This analysis is further developed infra Sections 6.3.3 and 6.3.4.

<sup>660</sup> The State Enterprise Law referred explicitly to this dynamic: to "the combination of interests of society, the collective and each worker" (article 1(2)); "the combination of centralised management and the autonomy of the enterprise" (article 1(2)); "the combination of interests of society, the collective and each worker" (article 2(1)); "democratic centralism and the combination of centralised management and



model of the industrial organisation. By recognising formally the existence and role of separate interests, the state enterprise was cut loose to sail upon the sea of the *perestroika* reforms, with the state hoping to retain control as it was blown upon uncharted waters by the winds of the participants and other interest groups.

### 6.3.2 *Incentivisation - the First Pillar (Full Khozraschet, Self-financing and Wages linked to Performance)*

In contrast with recessions in market economies, generally evidenced by a reduction in demand, the systemic problem in the Soviet command economy was traditionally based on a lack of sufficient supply (both in the amount and quality of production) to satisfy demand. This feature seemed to be ever present in the economy, even since the very earliest days of Soviet power. While the civil war was clearly responsible for the economic hardships of 1918-1919, during the NEP period the state sector continued to have problems in "competing" on equal terms with the market both in terms of production and marketing, despite Lenin's declaration that "we must learn to trade". Thereafter, the economy went through frequent systemic crises as Stalin pushed towards industrialisation. Rather than conceiving this issue in macro economic terms (ie as a systemic consequence of the command economy and state planning as a whole), it was generally problematised by the Soviet polity within the context of specific incentivisation measures and the need to provide better conditions to encourage the workforce to work harder and more efficiently, thereby resulting in additional output and improved quality. The two traditional strategies were differential wages and labour discipline.

The concept of paying differential wages in accordance with the quality and quantity of work was initially considered to be contrary to the Marxist principle of equalisation (ie distribution according to need). However, following the Brest Litovsk crisis, the state recognised specific incentivisation measures to be an indispensable part of Soviet economic policy, together with its twin, labour discipline. The 7<sup>th</sup> Party Congress in March 1918 acknowledged the need for "the most energetic, unsparingly decisive and draconian measures to raise self-discipline and discipline of workers and peasants".<sup>661</sup> At the same time, piece-rates and other forms of discriminatory payments were introduced.

The implementation of *khozraschet* in the early 1920s further consolidated the policy of differential wages because if an enterprise was to cover its costs, including wages, by its

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socialist self-management" (article 6(1)); "the interests of the state and the labour collective" (article 6(3)); and "planned management and observance of principles of full *khozraschet*, self-financing and self-management" (article 9(1)).

<sup>661</sup> Supra n.11, p.404.



revenues, then wages "by definition" would need to vary depending upon the level of revenues of the enterprise at which the workers were employed. While the policy of differential wages came to be broadly accepted, state control over wages in practice only developed in the late 1920s. Before the budget of 1925-26 there was no real control by Narkomfin over the allocation of salaries between staff. In its resolution of 2 January 1925, Sovnarkom recognised the need for a uniform nomenclature for posts and corresponding fixed salaries; and in 1925, uniform state regulation of wages of employees in state sector, including those on *khozraschet*, commenced and was gradually developed and extended throughout the following years.<sup>662</sup> By the end of the 1920s and with the defeat of Tomskey, the possibility for "collective bargaining" was reduced and wages became firmly integrated into the planned economy. In his famous speech, "The New Situation - New Tasks for Economic Construction", to the conference of business managers in June 22-23 1931, Stalin called finally to be "rid of this evil, equalisation must not be tolerated".<sup>663</sup> The unstable balance between discipline, incentivisation and central control remained, and throughout the 1950s and 60s various wage reform initiatives were pursued in an attempt to increase incentivisation and productivity.<sup>664</sup> These concerns even found expression in the Enterprise Statute and Production Statute of the confirmation model which contemplated the establishment of a material incentive fund, an enterprise fund and a wage fund.<sup>665</sup>

This traditional method of using wages as an incentivising strategy was also adopted during the early years of *perestroika*. In line with this policy, the Workers Wages Decree of September 1986<sup>666</sup> linked wage levels and bonus payments to specialisation and quality of output. Article 2 provided for the broadening of the rights of enterprises in "the stimulation of effective labour in new conditions of economic management, the perfection of management, the deepening of *khozraschet* and the transfer to new principles of self-financing". The autonomy of the enterprise in applying the proceeds of the labour fund was increased as well as "the role of the labour collective in the organisation of an efficient system of material and

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<sup>662</sup> Supra n.630, p.381-2.

<sup>663</sup> 13 Stalin 51.

<sup>664</sup> As Filtzer commented: "Since the early five year plans the Soviet regime has consistently failed to develop a coherent and workable system of incentives" (supra n.648, p.56).

<sup>665</sup> Enterprise Statute, articles 14 and 84; Production Association Statute, article 39.

<sup>666</sup> O Sovershenstvovanii Organizatsii Zarabotnoi Platy i Vvedenii Novykh Tarifnykh Stavok i Dolzhnostnykh Okladov Ravotnikov Proizvodstvennykh Otrasei Narodnogo Khozaystva, *Postanovleniya* (September 1986), no.1115, p.120. The preamble simply noted that "the current system of wages in many branches of the national economy does not satisfy the demands of acceleration of scientific-technical progress, transfer to intensive methods of economic management, increasing the quality of goods and does not correspond to a modern day level of organisation of production and labour".



moral stimuli". However, while the concept of self-financing was indeed broadened, the enterprise was still ultimately run by the state's appointed one-man manager, and the labour collective was merely involved in an ancillary way and in moral incentivisation.

The State Enterprise Law built upon these principles but rather than looking at wages in isolation, it constructed an organisation around the separate interests of the participants (the labour collective) more generally and thus wage policy became linked both to the profitability of the enterprise and to the rights of workers in management.

The organisational incentivisation regime of the 1987 state enterprises was founded upon three elements: (i) the enterprise was run on the basis of full *khozraschet* and self-financing; (ii) the residual income of the enterprise was available for distribution to the workers; and (iii) this distribution was effected on the principle of "distribution in accordance with work done".<sup>667</sup> The expressed intention was simple: to operate the enterprise with profit or revenue as "the solitary index of economic activity",<sup>668</sup> and to create a "deep personal interestedness of each worker in the economic use of all-people's ownership".<sup>669</sup>

***Full Khozraschet and Self-financing*** "Full *khozraschet* and self-financing" was a touchstone of the early *perestroika* reforms. It was contemplated expressly in the legislation of January 1987 on the contract-based concession enterprises as well as in the State Enterprise Law.<sup>670</sup> There was however no formal definition of the concept, and its origins and development can only be found in a series of unpublished decrees of 1985 - 1987.

The deepening role of *khozraschet* can initially be traced to the unpublished decrees that transferred enterprises and associations on a Ministry-by-Ministry basis to the so-called "new economic conditions". These transfers were carried out following, and on the basis of, Decree 669 of July 1985 "On Extending the Application of New Methods of Economic Mechanisms and Strengthening their Influence on the Acceleration of Scientific-Technical Progress".<sup>671</sup> Decree 669 was made by joint order of the Central Committee of the Communist Party and the Government of the USSR and aimed at extending the rights of enterprises and associations in planning and economic activity, and increasing "responsibility" for the results of their work. This was to be achieved by creating "genuine interestedness" of the labour collective in

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<sup>667</sup> State Enterprise Law, article 1(3).

<sup>668</sup> Ibid, article 2(2).

<sup>669</sup> Ibid, article 1(3).

<sup>670</sup> Supra Section 5.3.2.

<sup>671</sup> Only extracts of Decree 669 were published in the official gazette (*SP SSSR* (1985), no.23, item 115). For the unpublished version, see supra n.559.



the performance of the enterprise. Decree 669 can therefore be regarded as setting the basic parameters of the participation model.

Decree 669 was implemented in practice starting in October 1985 with Decree 981 "On the Transfer to New Economic Conditions of Production Associations and Enterprises of the Ministry of Medical Industry".<sup>672</sup> This decree was divided into three sections. The first section, "On the Perfecting of Planning", increased the role of the enterprise in the drafting of relevant plans. A basic index of items to be included in a five-year plan and in an annual plan were listed in the decree, and then individual enterprises were given the right to prepare drafts on the basis of "controlling" prices, limits and norms set by the Ministry. The second section of the decree was "On the Technical Perfecting of Production, [and on] Acceleration of Working out and Introducing of New Techniques"; and the third section was "On Increasing the Interestedness of the Labour Collective in the Growth of Effective Production and On the Strengthening of *Khozraschet*". It was in this third section that the positive law origins of full *khozraschet* and self-financing can be found. Increasing the interestedness of the workforce was to be achieved through a number of funds, including a wages fund, from which payments could be made to incentivise workers. The decree in this section gave further control over production activities and budget payments to the enterprise.

The transfer to "new economic conditions" was implemented broadly on the same basis in relation to enterprises in most other Ministries throughout the remainder of 1985 and continued into 1986.<sup>673</sup>

Following the decisions of the February XXVII Congress of the Communist Party, 1986 however was also to witness the start of a more radical policy that introduced explicitly the term full *khozraschet* and self-financing into Soviet subordinate legislation and prepared the foundations for its appearance in the primary and secondary legislation of 1987 (ie Decree 49 and the State Enterprise Law). In his speech to the XXVII Congress, Gorbachev called for the transition to "genuine *khozraschet*, self sufficiency and self-financing",<sup>674</sup> and on the basis of the decisions of this Congress, another series of unpublished decrees were enacted towards the

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<sup>672</sup> O Perevode na Novye Usloviya Kozyaisvovaniya Proizvodstvennykh Ob''edinenii i Predpriyati Ministerstva Meditsinskoi Promyshlennosti, *Postanovleniya* (October 1985), no.981, p.247.

<sup>673</sup> See Decrees 1073-1079 and 1094-1099 of 1985; and Decrees 1199-1209, 1321 and 1322 of 1986. Like Decree 981, these decrees were also unpublished in the official gazette and could only be found in the "*Postanovleniya*" books that were "for internal use only".

<sup>674</sup> Supra n.561, p.54.



end of 1986 and through 1987. This time these decrees provided for the transfer of enterprises and associations on a Ministry-by-Ministry basis to "full *khozraschet*".<sup>675</sup>

The first of these decrees was Decree 962 "On the Transfer of Associations and Enterprises of the Ministry of Chemical and Oil Machine Building of the USSR to Full *Khozraschet*".<sup>676</sup> The aim was to achieve "profitable" activity through increased accountability of the enterprise for the results of its production. Profit was deemed to be the most important economic indicator to be achieved through the establishment of efficient operations and autonomous control by enterprises over resources and revenues. The decree went on to include sections "On Expanding the Application of Economic Methods of Management", "On Improving the Organisation of Planning and Management", "On Expanding the Rights of Associations and Enterprises in Technical and Social Development", and, most importantly, "On Increasing the Interestedness of the Labour Collective in the Growth of Efficient Production and the Quality of Products" (which contained similar provisions to the equivalent section in the 1985/1986 decrees on transferring enterprises to new economic conditions).

As such, while the provisions of the State Enterprise Law in 1987 relating to full *khozraschet* and self-financing seemed like a radical departure from the regime of the confirmation model, in fact a transition had gradually been taking place since 1985 through the two sets of unpublished decrees, first on the transfer to new economic conditions and secondly on the transfer to full *khozraschet*. Therefore, the State Enterprise Law should be regarded as consolidating in primary legislation certain existing concepts rather than as introducing an entirely new set of economic norms.

The basic aims of full *khozraschet* and self-financing, although not explicitly stated in the State Enterprise Law, were therefore relatively clear: expenses were to be paid out of revenues; the "enterprise" was to determine "autonomously" the distribution of residual profits; and the enterprise was "obliged to work without showing a loss".<sup>677</sup> Therefore, within the framework of this adjusted planned economy, access to state subsidies by the enterprise was increasingly limited, but this was coupled with the gradual curtailment of the practice by the state of extracting all profits by administrative means, in excess of taxes, with a view to cross-subsidising other enterprises operating with the planned economy. The finer points of

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<sup>675</sup> See Decrees 962-965, 1072 and 1282 of 1986 and Decrees 665, 874, 906-911, 916, 937-944 and others of 1987. Again, copies of these decrees can only be found in the "*Postanovleniya*" books for internal use only.

<sup>676</sup> O Perevode Ob''edinenii i Predpriyatii Ministerstva Khimicheskogo i Neftyanogo Mashinostroeniya SSSR na Polniy Kozyaistvennyi Raschet, *Postanovleniya* (August 1986), no.962, p.111.

<sup>677</sup> State Enterprise Law, article 17(4).



the application of full *khozraschet* and self-financing in practice were as much a question of politics and economics as of law.<sup>678</sup>

Under the new concept of "full" *khozraschet*, a guaranteed minimum wage was questioned with the introduction of a system under which wages were paid only from the revenues/profit of the enterprise (following statutory deductions, taxes and other expenses); and where the residual profit was distributed among the workers depending upon their individual "labour contributions". Like the basic concept of identifying "a participant" and its interests as separate from that of the state, this framework for the payment of wages was also indebted to collective farm law, and in particular, payments made from residual revenues distributed on the basis of labour days worked.<sup>679</sup>

*The Nature of Residual Income* The State Enterprise Law provided two alternatives for calculating the residual amount, called the "*khozraschet* revenue of the collective" (ie the residual profit after statutory deductions, taxes and expenses).<sup>680</sup> Article 3 provided that "the *khozraschet* revenue of the collective, the source of the production and social development of the enterprise, the payment of labour, shall be located at the disposal of the enterprise, shall be used autonomously and shall not be subject to seizure".

This concept of *khozraschet* revenue as described in article 3 was problematic and illustrated again the tensions in distinguishing between an anthropomorphic enterprise and the labour collective.<sup>681</sup> On the one hand, it referred explicitly to *khozraschet* revenue as being "*of the collective*" (and not of the state (who was the legal owner of the enterprise and its property)

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<sup>678</sup> Despite these basic rules, there were instances where state assistance continued to be contemplated, most particularly in the area of credits. An enterprise was given the right to open bank accounts and use bank credits but, in accordance with article 18(1), a "systemic failure" to repay loans resulted in the loss of the right to receive new credits. However, article 14(4) provided that if an enterprise did not have sufficient assets to pay for goods ordered and could not receive bank credits, the state superior agency was obliged to allocate funds from central resources to that enterprise, on condition that they were repaid at some future date (ie they were construed in strictly legal terms as a loan and not as a "subsidy"). Furthermore, article 18(1) actually contemplated the issue of a state superior agency guarantee as an exception to the rule that systemic failure to repay loans would result in the loss of the right to receive bank credits. Finally, although there was the possibility to liquidate a state enterprise in financial difficulties (see *infra* Section 6.3.4.2), the procedures involved would have made this difficult to achieve in practice.

<sup>679</sup> See *supra* Section 2.4.1 and *infra* Section 6.4.2. Ultimately, however, this concept (like the notion of participation itself) can be traced to the Brezhnev Constitution. This was recognised in article 14(1) of the State Enterprise Law which provided: "At the enterprise, a citizen of the USSR shall realise his constitutional right to work and to be paid in accordance with the results of their labour, its quantity and its quality").

<sup>680</sup> "On the basis of normative distribution of profit" and "on the basis of normative distribution of revenue received after compensation from receipts of material expenses" (article 3(1)).

<sup>681</sup> See discussion at n.654 and associated paragraphs.



nor of the enterprise itself). This was consistent with the notion of the labour collective as "proprietor", because the entitlement to residual profits normally rests with the ultimate "proprietors" (or "economic owners") of a juridical person. On the other hand, while the state was clearly prevented from "seizing" this *khozraschet* revenue, its disposal was to be decided *by the enterprise* "autonomously" (ie not by the labour collective).<sup>682</sup> Finally this definition suggested that the "*khozraschet* revenue" was not just to be used for "the payment of labour", but also for the "production" and "social development" of the enterprise.<sup>683</sup> It may be that this division between the right of the worker to the *khozraschet* revenue and the right of the enterprise to distribute it, was the first indication under Soviet law (although somewhat imperfectly) of the ownership-control distinction and of the right of owners (who later became stockholders) to dividends, but the right of management (who later became directors) to decide on whether to declare any dividends. The wider use of the *khozraschet* revenue for purposes other than just the payment of labour again has parallels with the status of residual income as the source for dividends. The decision to use the residual income for making dividend payments to participants, or alternatively for use to invest "in the enterprise", was made at the discretion of the management.

***Distribution of Residual Income*** From the residual profit (the *khozraschet* revenue of the labour collective), wages were to be "determined by the final results of work, [and] by the worker's personal labour contribution ("*vkladom*")".<sup>684</sup> Article 14(2) gave "the enterprise" the right, "on the basis of openness" and "objective evaluation", to determine how individual "contributions" were to be assessed and translated into a wage (ie the portion of this residual profit to be allocated to a particular worker). It was noted explicitly in the State Enterprise Law that there was to be no maximum cap on the amount that could be earned. Within the context of "established norms", the enterprise was given wide discretion in establishing wage funds for specific categories of worker, new base salary rates, forms and systems of wages and incentive funds.<sup>685</sup> However as a procedural "check", and by way of ensuring that the enterprise was managed by taking into account a combination of interests, the council of the

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<sup>682</sup> The right of "the enterprise" to distribute the *khozraschet* revenue was also provided by article 2(2).

<sup>683</sup> This use of the *khozraschet* revenue was reinforced by article 3(1) which noted "the *khozraschet* revenue of the collective as the main source of self-financing of its [the enterprise's] production and social development and of payment for work [of workers]".

<sup>684</sup> The term "*vklad*" presumably meant the worker's physical efforts rather than any contribution in the sense of a payment (in cash or in kind) to the enterprise. It therefore had a different meaning to that used in the context of the contract-based concession model (see *supra* Section 5.4.2.1). The term "labour contribution" was also used in connection with the profit distribution rules of the second expression of the participation model (see Cooperatives Law, article 13(1), and *infra* Section 6.4.2).

<sup>685</sup> State Enterprise Law, articles 14(4) and 14(5).



labour collective was additionally given the right to ensure that "payment for the work of the workers corresponds to their personal contribution and the fair distribution of social wealth".<sup>686</sup>

Therefore the "enterprise" had the power to decide whether to apply the residual income towards the payment of wages; if so, what portion should be distributed in wages; and the division of that portion between workers on the basis of their individual labour contributions. If, as has been argued, the "enterprise" (ie one man manager) was to act in the combined interests of the state and the "workers (participants)", the State Enterprise Law meant that the internal economic framework of the industrial organisation had been radically restructured. The state's unitary monopoly interest of the confirmation governance model had been diluted by the presence of a new separate and independent interest, and the State Enterprise Law expressly acknowledged that interest and explicitly aimed at passing back to the participant an element of economic and managerial control in the pursuit of efficiency and profitability.

### 6.3.3 *Democracy - the Second Pillar (The Combination of Centralised Management and Socialist Self-Management)*

The democracy principle in the Soviet economy and polity had been gradually extinguished during the 1920s as Stalin took control over the Communist Party and extended its hegemony over the voices of opposition. As Trotsky had feared in his speech to the 12<sup>th</sup> Party Congress, "party democracy" gave way to the "nomination principle" and "secretarial bureaucratism", a movement that can be dated to the appointment of Kaganovich in April 1922 to head Uchraspred (the section of the secretariat in charge of qualifications of party personnel). A classification of posts was established by Orgburo in October 1923, and Orgburo and Uchraspred worked together in the proliferation of the nomination system until their amalgamation in 1924. The development of the Communist Party as a mass political party based on the principles of dictatorship and run by the secretariat and politburo under the leadership of the general secretary was achieved by 1930;<sup>687</sup> and the 16<sup>th</sup> Party Congress of

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<sup>686</sup> Ibid, article 7(1).

<sup>687</sup> The condemnation of fractionalism began at the 10<sup>th</sup> Party Congress of March 1921. During Lenin's illness, the triumvirate defeated the "platform of the 46" by December 1923 thereby consolidating control over Pravda and the party in Moscow and the regions; the 1924 USSR Constitution furthered the process of centralisation; local administrations were established in the context of the campaign of the mid-1920s to revitalise the Soviets; by the 14<sup>th</sup> Party Congress, control had been taken over the Leningrad party, and Komsomol as an independent party organ had been tamed and transformed into the junior branch of the Communist Party; the defeat of the united opposition was achieved by 1927 and the development of an independent trade union movement under Tomsy's leadership was quashed by mid-1929.



June-July 1930 was the first in Soviet history where there was no opposition to any aspect of official policy.

In the industrial economy, political dictatorship was replicated within the organisational forum through the principle of "one-man management".<sup>688</sup> While there had been much ideological lip service paid to the role of the "collective" as the heartbeat of the state enterprise, most traditionally built upon the work of Venediktov and Bratus, it was more the work of Tolstoy, and his concept of the "theory of the director" as the essence of the state enterprise, that reflected reality.<sup>689</sup> The main "formal" exception to the dictatorship principle in the wider Soviet economy was to be found in the agrarian economy where the legacy of collectivisation had resulted in a compromise in the legal structure of the collective farm. The artel form was therefore expressed to be based on "collective farm democracy".<sup>690</sup>

The resurrection of the "participant" as an independent "interest" in the 1987 State Enterprise Law required that the participant not only had the right to receive a part of residual profits in proportion to work done, but also that the participant had the ability to determine the overall level of those profits both through his labour contribution as well as through a voice in management decisions. The State Enterprise Law recognised the interaction between these first two pillars of the participation model by providing that "the enterprise's activities on conditions of full *khozraschet* and self-financing shall be carried out in accordance with the principle of socialist self management".<sup>691</sup>

While the concept of self-management encouraged the "interestedness" of the participant in decision making, the regime of "*socialist* self-management", like the principle of "collective farm democracy", entailed a continued involvement of the Soviet state. Therefore the notion of a balance was expressed in article 6(1): "the management of the enterprise is carried out on the basis of the principle of democratic centralism and the combination of centralised management and socialist self-management of the labour collective".

This balance gave rise to three formal institutions of management: the one-man manager; the general meeting (conference) of the labour collective; and the council of the labour collective. In addition, there were certain limited instances where other "political" and "social"

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<sup>688</sup> See supra Section 2.2.

<sup>689</sup> Yu.K. Tolstoy, *Soderzhanie i Grazhdansko-Pravovaya Zashchita Prava Sobstvennosti v SSSR* (Leningrad:1955/6), p.60-92.

<sup>690</sup> See supra Section 2.4.1.

<sup>691</sup> State Enterprise Law, article 2(3).



organisations were involved in the management process, including the Komsomol and the Communist Party (the latter described as "the political core of the collective").<sup>692</sup>

Although the concept of "one-man management" remained, and with it the logic of a single point for interest-group capture, this traditionally "dictatorial" feature was adjusted to take account of the new compromise. As has been argued, no longer was the one-man manager to be conceived to be the single delegate of the unitary state; instead the manager was directed to "express the interests of the state and the collective" and was to be "responsible for the results of the enterprise's work to the state and the labour collective".<sup>693</sup>

The process of the manager's appointment also reflected this new balance. The nomination principle of the confirmation model gave way to more democratic elements: the general meeting of the labour collective voted on the appointment of the one-man manager and this was confirmed by the state superior agency. The state superior agency was only given negative control. If the state superior agency rejected an elected one-man manager, a new election was held and the state superior agency had to give reasons for its rejection. This therefore introduced an element of accountability and transparency, checking the possible capricious use of the state superior agency's veto right.

Once appointed, the balance shifted further in favour of the labour collective: the one-man manager could only be dismissed by the state superior agency following a decision of the general meeting or council of the labour collective.

The express powers of the one-man manager, and as representative of "the enterprise", were pervasive. These included the power to represent the enterprise, conclude contracts, sell property, issue binding instructions and deal with the enterprise's personnel. In addition, the State Enterprise Law suggested that the strict civil law *vires* regime of the confirmation model was in some way to be relaxed because the enterprise was given the "right at its own initiative to adopt all decisions, if they are not contrary to prevailing legislation".<sup>694</sup>

The interests of the labour collective were expressed not only through this new understanding of the one-man manager (as elected by the labour collective and as a representative of their interests as well as those of the state), but also specifically through the general meeting (conference) of the labour collective. The general meeting was given additional powers

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<sup>692</sup> State Enterprise Law, article 6(1). See also *supra* n.566.

<sup>693</sup> State Enterprise Law, articles 6(3) and 6(4).

<sup>694</sup> State Enterprise Law, article 2(5). This seemed to hint at the introduction of a permissive regime in contrast to the prevailing authorisation regime of rights embodied in civil law doctrine (see Section 7.4.1 and *infra* n.922).



including the right to examine and confirm enterprise plans, and to approve the collective contract and other important questions of the enterprise's activity.

The final management organ, the council of the labour collective, was intended to be the plenary institution of the general meeting (conference) of the labour collective, convened in the periods between general meetings. In the same way that the concept of "balance" was introduced in developing the "new" concept of the one-man manager (as a representative of the labour collective's interests as well as the state's), the concept of "balance" was also introduced in a "new" concept of the council of the labour collective: this time the council was required to take into account the state's interests, as well as those of the labour collective. On this basis, the State Enterprise Law directly contemplated the election of representatives of management, the Communist Party, Komsomol and other public organisations to the council; however the number of management representatives was limited to a quarter.<sup>695</sup> The role of the council included monitoring the fulfilment of decisions of the general meeting; implementing any comments and proposals of workers; hearing management reports; solving questions of improving management and organisational structure; and confirming conditions of socialist competition (together with Communist Party, Komsomol and trade union organisations). The decisions of the council, within its competence, were expressed to be binding on the management and members of the collective.

The procedural rules governing the internal governance democratic processes were rudimentary. The election of the one-man manager was expressed to be "as a rule on a competitive basis" (Soviet "elections" traditionally involved only one candidate), by a secret or open ballot of the general meeting of the labour collective, for a 5 year term. The election of the council of the labour collective was also to be by a secret or open ballot of the general meeting of the labour collective, for a 2 or 3 year term. At each election, at least a third of the members of the council were generally required to be newly elected. Council sessions were required to be held at least once a quarter.

The procedures were not much more developed than as summarised in the previous paragraph.<sup>696</sup> However, irrespective of the brevity of these provisions in the 1987 State Enterprise Law, they, like the provisions relating to full *khozraschet* and self-financing, were immensely significant. An internal management structure had been introduced that tempered

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<sup>695</sup> State Enterprise Law, article 7(3).

<sup>696</sup> The lack of detail may have been due to the legacy of the confirmation model. In the context of that model the legislation only had to contemplate one interest within the management regime, and a one dimensional manager which expressed that single interest. There was thus no need for complex and detailed provisions on internal management or governance.



centralised management with socialist self management by the labour collective and which required "the participation of the entire collective and its social organisations in the working out of very important decisions and control over their fulfilment".<sup>697</sup> The State Enterprise Law represented the first attempt since the 1930s to develop democratic procedures within the domestic industrial organisation based on the recognition of more than one interest. It was the introduction of "the other" into the industrial organisation upon the foundations laid by the State Enterprise Law that became the catalyst for the radical restructuring of the economy some years later in Spring 1990.

#### 6.3.4 *Coercive Law and Governance in a Regime of Separate Interests*

The identification of separate interests within the organisational forum and the granting to them of democratic means of expression resulted not just in a compromise in terms of the operation of the internal management organs, but also in terms of economic theory. The policy of encouraging participants to pursue their "own" interests was developed in the hope that this would result in overall efficiency gains for the Soviet national economy as a whole (on a Smithean type analysis). However, the principles underlying such an approach were mutually exclusive to the Stalin form of socialist planning and the unity of interests expressed in the concept of the all-people's state. As such, this policy was tempered, not just by requiring that the interests of the labour collective (ie the participant) be combined with those of the state, but also by formally constructing the enterprise as an organisation that had responsibility for the social as a whole (and not just as an instrument for the pursuit of the interests of the participants).

Article 1(3) specified "the principal task" of the enterprise as "the satisfaction in every way of the social requirements of the national economy and citizens in its products (works, services) with a high level of consumer properties and quality with the minimum of the expenses, increasing the contribution to the acceleration of social-economic development of the country and, on this basis, ensuring the growth of the well-being of the collective and its members. The requirements of consumers *shall be binding* upon enterprises and their full and timely satisfaction - this is the highest meaning and norm of the activities of each labour collective".<sup>698</sup>

Clearly the protection of these wider interests could not have been achieved through the narrow governance regime of the 1987 state enterprise because there were only very limited

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<sup>697</sup> State Enterprise Law, article 6(1).

<sup>698</sup> State Enterprise Law, article 1(3) [emphasis added].



possibilities for the involvement of representatives of the wider social in the three management organs. As such, protection of the interests of the "national economy and citizens...and...consumers" was sought through coercive law, binding requirements, and traditional governance strategies.

#### 6.3.4.1 *Coercive Law*

While in later expressions of the participation model the logic of the separation of interests resulted in the erosion of the basic features of the confirmation governance regime itself, the state's position as legal sovereign always remained. As such, this position came to be exploited through the proliferation of coercive law. Although coercive law had been an element of the confirmation model,<sup>699</sup> within the participation model, it became the central governance technique of the state, and hence can be viewed in its own right as the third pillar of the participation model. Therefore, for example, aware that the interests of the wider social could not have had a specific voice in the management organs of the enterprise, the state, by legislative diktat, simply "defined" the "principle task" of the enterprise in the State Enterprise Law in terms of the satisfaction of the social requirements of the national economy, and hence "obliged" the enterprise (ie its management) to take into account the interests of the social in its management decisions.

The origins of coercive law can perhaps be dated back to the labour law of the years of war communism and the regulations of the 4<sup>th</sup> All-Russian Congress of Soviets which introduced a strict regime of labour discipline. Rather than creating structural economic incentives to encourage efficient and hard work, the approach taken by the 1918 RSFSR Labour Code was to conceive of "work" as a general obligation, a debt owed to society for the advancement of the socialist state, and as such "required" it to be carried out by way of legal diktat. The attendant "state militarisation of labour" was developed through the state labour exchanges, labour books, and forced labour camps for offenders of labour discipline. As Carr explained, "the ultimate result of war communism in the field of labour policy was to leave no other incentives in operation except revolutionary enthusiasm and naked compulsion".<sup>700</sup>

Naked compulsion was used by the early Soviet regime throughout its industrialisation effort and beyond, both in terms of labour law, grain requisitioning and requirements for the regime of economy. The legacy of this approach, the use of coercion rather than systemic incentives, survived into the provisions of the State Enterprise Law where enterprises were simply

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<sup>699</sup> Supra Section 3.4.3.

<sup>700</sup> Supra n.217 (1952), p.218.



"obliged" ("*obyazano*") or "required" ("*dolzhna*") to operate in a certain manner, or to take into account certain wider interest groups.<sup>701</sup> The use of the present tense in the Russian language in legislation is generally translated as "shall", implying the imposition of an obligation. In addition to the use of the terms "oblige" or "require", there were numerous examples in the State Enterprise Law of the use of a verb in the present tense where the subject was "the enterprise".<sup>702</sup> The obligation in whatever form was then sometimes even specifically coupled with prescribed penalties.<sup>703</sup>

In addition to the use of its position as legal sovereign to exploit the possibility for coercive law, in this first expression of the participation model, the state also retained the other elements of the governance regime of the confirmation model through its positions as state-creator-owner, property-owner, and economic sovereign. Not only did the State Enterprise Law broadly leave all elements of the confirmation governance regime intact, but it also explicitly aimed at "strengthening state (all-people's) ownership",<sup>704</sup> and still conceived of the economy as a state-run indivisible complex.<sup>705</sup> It was only the "unintended" consequences of creating a regime based on the separation of the interest of the participant from that of the state that led eventually to the gradual erosion of these other elements of the traditional governance regime as evidenced in the later expressions of this model.

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<sup>701</sup> As in the confirmation model, the State Enterprise Law provided for coercive micro management by legislative diktat of essential economic operations of the enterprise which, in a market economy, would have been regulated by civil law and general economic structural incentives. For example the State Enterprise Law provided that: "the activities of the enterprise must not violate normal conditions of work" (article 2(5)); "the enterprise shall be obliged to permanently ensure the reproduction of the material-technical base on a progressive basis, to effectively use of production capabilities and basic funds" (article 4(1)); "the enterprise shall be obliged to ensure safe keeping, the rational use and accelerated turnover of circulating assets" (article 4(3)); "the enterprise shall be obliged to comply strictly with planning discipline and fully fulfill plan and contractual obligations" (article 10(5)); "the enterprise shall be obliged to ensure the strict compliance with technological discipline, standards, technical specifications and reliability, trouble-free and safety in the use of equipment produced by it" (article 11(3)); "the enterprise shall be obliged to give the utmost importance to activating the human factor, improving work conditions, increasing the creative content of work, gradually transforming labour into a prime necessity for life" (article 13(2)); and "the enterprise shall be obliged to settle accounts in a timely manner" (article 18(2)).

<sup>702</sup> Almost every economic activity of the enterprise was provided for. For example: "the enterprise shall display constant concern for the steady growth of vocational skills...of its personnel" (article 8(2)); and "the enterprise shall carry out the technical re-equipment, reconstruction and expansion of existing production facilities by efficiently combining do-it-yourself and contract methods" (article 12(4)).

<sup>703</sup> See *infra* Section 6.3.4.3.

<sup>704</sup> State Enterprise Law, preamble.

<sup>705</sup> The State Enterprise Law referred to the economy as "a single whole" (preamble), a "single national-economic complex" (article 1(1)). See *supra* n.567.



#### 6.3.4.2 *Creation and Termination*

Due to the continued existence of the role of the state as "creator-owner", the law regarding the creation and termination of the 1987 state enterprises differed little from that of the 1965 state enterprise.<sup>706</sup> There was only one sentence in the entire State Enterprise Law that mentioned the procedure for their creation and this simply stated: "enterprises shall be created in accordance with the procedure established by the USSR Council of Ministers".<sup>707</sup> The law also provided that each enterprise should have a charter which included the purpose of its activities and a seal.<sup>708</sup>

As regards their termination, the law blurred the traditional distinction made in the civil codes between liquidation and reorganisation as the two types of "termination".<sup>709</sup> By contrast, it provided for reorganisation (through merger, accession, separation, division, transformation) and termination (or liquidation).<sup>710</sup>

The categories of division and transformation were entirely novel, as the civil codes only contemplated reorganisation through merger, separation or accession. "Transformation" was particularly important as this implied that state enterprises had the capability of being "transformed" into a different type of juridical person. In 1987 it would have been difficult to have identified the form of such transformed entities (other than cooperatives). However, the introduction of such a concept provided the first hint of the subsequent development of the de-statisation programme and the ability to lease a "state enterprise" thereby "transforming" it into a "leased enterprise".<sup>711</sup>

In contrast with the confirmation model, which was silent as to the circumstances and procedures for liquidation, the State Enterprise Law focused more carefully on this concept and set out certain specified circumstances when termination (or liquidation) was possible. These were when: (i) there was no further need for the enterprise's operations and it could not be reorganised; or (ii) in other instances specified by legislation; or (iii) when the enterprise was operating at a loss for a long time *and* when it was insolvent *and* when there was an absence of demand for its products *and* in the instances when measures had been taken by the

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<sup>706</sup> See supra Section 3.2.

<sup>707</sup> State Enterprise Law, article 23(1).

<sup>708</sup> State Enterprise Law, article 23(3). The importance of a purpose clause for the law on *vires* is discussed supra Section 3.4.1.

<sup>709</sup> See supra Section 3.2.

<sup>710</sup> The State Enterprise Law seemingly used the words termination ("*prekrashchenie*") and liquidation ("*likvidatsiya*") interchangeably (see articles 23(1) and 23(2)).

<sup>711</sup> On the leased enterprise generally, see infra Section 6.5.



enterprise and its state superior agency to improve profitability which had not yielded results.<sup>712</sup> Additionally, if an enterprise systematically violated "payment discipline", the law provided that its bank had the right to declare the enterprise insolvent and to communicate this to its basic suppliers and the state superior agency.<sup>713</sup>

The possibility of termination was therefore expressed for the first time in a law of the later Soviet period to be available upon the occurrence of financial difficulties. Although the State Enterprise Law provided for a number of cumulative conditions precedent to be satisfied (operation at a loss, insolvency, no demand and unsuccessful remedial measures adopted) as well as the obligation to find new jobs for, or retrain, employees made redundant,<sup>714</sup> these provisions still evidenced an initial attempt to impose some financial boundaries upon the continued operation of state enterprises and to develop in practice the declaration in article 2(2) of the State Enterprise Law that "profit or revenue shall be the solitary index of economic activity of the enterprise".

#### 6.3.4.3 *State Ownership of the Enterprise, Juridical Personality and Responsibility*

In the elaboration of the new framework which contemplated a "combination of interests", certain aspects of the drafting of the State Enterprise Law may have suggested that a new regime of ownership relations was being developed. However it is unlikely that any of the "ambiguities" in the drafting actually resulted in, or were intended to result in, a new ownership regime.

It seems that the basic problem resulted from the fact that the regime of balancing interests had been taken from collective farm law. The collective farm, in contrast to the state enterprise, had the right of collective farm-cooperative ownership independent from state ownership. Therefore, when the first two pillars of the participation model were incorporated from collective farm law into the confirmation model, this put pressure on the coherence of the existing ownership regime (or lack thereof) of the industrial organisation.

The argument that the existing state ownership regime of the confirmation model may have been compromised by the provisions of the State Enterprise Law is based on the status given in the State Enterprise Law to the labour collective as the "fully-fledged proprietor

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<sup>712</sup> State Enterprise Law, article 23(1).

<sup>713</sup> The basic suppliers then had the right to stop deliveries and the state superior agency was obliged, together with the enterprise, to adopt measures to remedy the situation and restore accounting discipline. (State Enterprise Law, article 18(3)).

<sup>714</sup> State Enterprise Law, article 23(2).



("khozyain") of the enterprise", "using, as proprietor, all-people's ownership".<sup>715</sup> The phrase "fully fledged proprietor" was particularly significant as this was the phrase used in the Cooperative Law to describe the place of the cooperative which clearly did have the right to own property.<sup>716</sup> It is probable however that these references were simply ideological lip service to the acknowledgement of the separate interest of the labour collective and that the existing regime of the confirmation model was to be left intact.

The other provisions of the State Enterprise Law which described the ownership regime of the 1987 state enterprise suggested that, irrespective of the professed role of the labour collective as "proprietor", the state was intended to remain the legal owner of the enterprise and its property, which continued to be allocated to the enterprise by way of operative management. Article 1(2) of the State Enterprise Law referred to the enterprise as having the right to "possess [ie not own] a solitary part of all-people's ownership and have a separate balance sheet". This was then expanded in article 4(1) which gave the enterprise "the right to possess, use and dispose of this property".<sup>717</sup> Furthermore, the State Enterprise Law retained references to property "of the enterprise" (rather than in "the ownership of" the enterprise).<sup>718</sup> All of this terminology was broadly drawn from the current regime of state ownership-operative management and the reference to "proprietor" should be understood in this context. Furthermore, there were no explicit references to the right of ownership of the enterprise, or of the labour collective acting as legal "owner" (in addition to proprietor). Thus, while the logic of the collective farm compromise may have nudged the participation model towards contemplating a new form of ownership relations, the 1987 State Enterprise Law still placed the ownership framework firmly within the former regime of confirmation model: hence the 1987 state enterprises were juridical persons without the independent right of ownership and were still considered as indivisible objects located "in" state ownership allocated state property by way of operative management.

As the basic juridical characterisation of the state enterprise remained unchanged in the 1987 law, the responsibility regime of the confirmation model was also seemingly left intact. Therefore, as a matter of principle, the State Enterprise Law separated responsibility for the

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<sup>715</sup> State Enterprise Law, articles 2(3) and 1(2).

<sup>716</sup> Cooperatives Law, article 7(4). See *infra* Section 6.4.4.2.

<sup>717</sup> The concept of operative management encompassed this triad of rights; however, in contrast to the right of ownership, these rights in the case of operative management were limited by additional restrictions that were placed by the owner. See *supra* Section 2.3.1.

<sup>718</sup> This formulation using the genitive case, without specifically mentioning "in the ownership of", was used when indicating the existence of solitary or separated property, without the right of ownership in such property.



debts of the enterprise from responsibility for the debts of the state and vice versa. However, the introduction of "financial indicators" in the determination of solvency and the importance of profitability generally may have further evidenced a trend in the law from a regime of autonomous property responsibility to one based on "liability".<sup>719</sup> This embryonic development towards a liability based regime developed the steps already taken in this direction as contemplated in the contract-based concession model where full *khozraschet*, self-financing and non subsidy were the foundations for a regime where "all" assets were available for execution by creditors.

In addition to suggesting a move towards a liability regime through the introduction of liquidation in the case of financial difficulties (crucial for any understanding of limited liability), the State Enterprise Law hinted more generally at a move towards a "fuller" concept of responsibility. Building upon the role of the enterprise as an expression of wider social interests, the ambit of the concept of responsibility was broadened beyond the narrow liability context.<sup>720</sup> Article 2(5) provided that the enterprise was to bear "full responsibility" ("*polnaya otvetstvennost'*") for compliance with the interests of the state and rights of citizens, for the safekeeping and development of socialist ownership, for the fulfilment of obligations, for the ensuring of profitability and of full *khozraschet*, and for the strengthening of state, production and labour discipline.

This wider concept of responsibility was given specific application in a number of instances where legislative coercive diktat was coupled with attendant sanctions so that, for example, article 11(5) obliged ("*obyazano*") research organisations to ensure that their work corresponded "to the basic indicators of the highest world standards". In the event that they did not, the organisation would bear "material responsibility" and the managers and development personnel would be subject to "disciplinary responsibility, lose wages and material incentives". Thus the concept of "full" responsibility "required" a high quality of research, and failure resulted in material penalties. Other examples included the obligation to fulfil contractual delivery requirements, or else bear "economic responsibility" (article 15(2)); and the obligation to fulfil contractual terms generally, or else "bear economic responsibility" and pay compensation for damage caused (article 16(3)). Apparently legislators were not

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<sup>719</sup> On the differences between "autonomous property responsibility" and "limited liability", see *supra* Section 3.3.

<sup>720</sup> This development of a wider concept of responsibility was further developed in the 1988 Cooperatives Law (which, like the contract-based concession model, included basic assets in the assets available to creditors, notwithstanding the fact that the civil codes isolated them from execution) and in the 1990 Law on Enterprises which introduced explicitly the concept of "full property responsibility" (see *infra* Sections 6.4.1 and 7.5.4.3).



comfortable with leaving the question of responsibility and the assessment of the level of damages to the general civil law of contract. While the participants were encouraged to pursue their own narrow interests, it perhaps was feared that these may not have been coincident with those of the wider national economy. As such, the state as legal sovereign used coercive law to compel behaviour and introduce "fuller" social responsibilities where structural incentives may have been absent.

#### 6.3.4.4 *Economic Sovereign*

The role of the state as economic sovereign (like the role of the king in the feudal system) was derived from its monopoly ownership of the means of production and hence its ability to "administer" the economy as a whole through the plan. Even collective farms fell within this single national economy, and the ownership structure of collective farms finessed the question of the identity of their ultimate owner, thereby posing no challenge to the state's economic hegemony.<sup>721</sup>

Despite the fact that both the fragmentation of the single all-people's state through the acknowledgement of the separate interests of the participants, and the development of enterprise autonomy, attacked and undermined the basic assumptions on which the state's economic sovereignty was based, there was no intention of compromising the scope of the state's basic economic sovereignty through the adoption of the State Enterprise Law. On the contrary, the State Enterprise Law was intended to "improve" socialist planning.

The preamble to the State Enterprise Law stated that the law was to determine "*the economic and legal basis of the economic activity of the socialist state enterprise*" [emphasis added] and for this reason the law was concerned as much with the operation of the state enterprise within the national economy (including the developing of its production plans, production quality and material and technical supply) as with its legal characteristics. The State Enterprise Law provided a regime that attempted to preserve the planned economy while at the same time promoting increased decentralised autonomy of the enterprise. Gorbachev explained the law as "completing the construction of a modern model of socialist economy to meet the challenge of the present stage of national development...[where] the advantages of planning will be increasingly combined with stimulating factors of the socialist market".<sup>722</sup>

The State Enterprise Law again adopted the framework of "combining interests" in elaborating the place of the enterprise within the command economy, and went on to limit the

<sup>721</sup> On the ownership regime of the collective farm, see *supra* Section 2.4.2 and *infra* Section 6.4.1.

<sup>722</sup> *Supra* n.533, p.87, 90.



scope of "its" autonomy. The basic rule was set out in article 2(1) which provided that "the activities of enterprises are built on the basis of the state plan of economic and social development as an important instrument in the realisation of the economic policy of the Communist Party. Directed by controlled prices, state orders, long term scientifically substantiated economic norms and limits, as well as the orders of consumers, the enterprise shall autonomously work out and confirm its plans and conclude contracts".

Therefore the relationship between the superior state agency and the enterprise was one of relative autonomy in the Althusserian sense. The state would set the broad parameters on the basis of which the enterprise would develop operations. The state clearly had the upper hand in this balance as it retained the ultimate right to elaborate general plans for the economy on the basis of which the specific plans of the enterprise were then elaborated; the right to establish prices centrally; the right to require compliance with state orders promulgated in accordance with the plan; and the right to establish long term economic norms. However, in certain specific areas, the law also recognised the interest of the enterprise and generally provided a limited balance. For example, planning was expressed to be based on democratic centralism and the enterprise had the right to develop its plans autonomously. Prices that were not fixed centrally were permitted to be set by the enterprise alone or as negotiated with the customer.

#### ***6.3.5 The State as Defendant and the Significance of the First Expression of the Participation Model***

The first expression of the participation model did not develop a new economic system. In fact the intention was quite the opposite. It was directed at adjusting the framework of the industrial organisation in order to perfect further the existing socialist economy. As such, the ownership and governance regimes of the confirmation model were broadly unchanged.

However, the 1987 State Enterprise Law did introduce a principle that was to lead ultimately to the dismantling of the very system it was intended to support. In attempting to incentivise the participants (the labour collective), the legislation recognised the role, goals and rights of the labour collective as an independent interest, separate from that of the state. The State Enterprise Law embraced the collective farm compromise and thereby admitted the separation of the private from the public into the industrial economy and so questioned the very foundation of the concept of the all-people's state.

If the restructuring of the economy was to be meaningful, as Gorbachev was determined it would be, the rights given to the participants would be required to be more than simple



legislative lip-service. Workers would have to feel their "deep personal interestedness...and...participation"<sup>723</sup> in a real way. Hence the first two pillars of this model, incentivisation and democracy, would need to be policies that had effect in practice. To this end, the State Enterprise Law incorporated the possibility for legal redress for participants where a state superior agency had abused its position or exceeded its competences. In the past, legislation contemplated the possibility for compensating payments but there was no means of enforcing these rights.<sup>724</sup> By contrast, the State Enterprise Law first increased transparency by requiring the superior state agency to give reasons when exercising discretions (eg in vetoing the appointment of the one-man manager); and then provided that if a ministry, department or other state superior agency issued an act that was *ultra vires* or breached legislative requirements, then the enterprise had the right to appeal to an arbitrazh court to have the act declared invalid in full or in part. Furthermore, an enterprise had the right to be compensated for losses caused in attempting to comply with such acts, or with acts that violated the rights of the enterprise.<sup>725</sup> In short, state agencies bore "responsibility" for their failure to comply with the provisions of the State Enterprise Law.<sup>726</sup> In this way the 1987 State Enterprise Law developed the very embryonic roots of the framework of the rule of law state, where law was not just the tool of the state but actually bound the state by giving others legal rights against the state.

The State Enterprise Law, as the first expression of the participation model, presented a new foundation for a new organisational form, one which separated the private from the public and gave the former legal rights against the latter. Developed on the basis of identifying the participant and giving him the right to receive wages linked to performance and the right to participate in management, this model contained the seeds of the destruction of the planned economy which it was intended to support. Further expressions radicalised this foundation by first excluding the state from the ownership regime, thereby undermining the foundations of the governance system of the confirmation model, and then by reorientating the relations between the participant and state from the realm of administrative/economic law to one based primarily in the civil law of contract.

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<sup>723</sup> State Enterprise Law, article 1(3).

<sup>724</sup> Supra n.21, p.257.

<sup>725</sup> State Enterprise Law, article 9(3).

<sup>726</sup> State Enterprise Law, article 24.



#### 6.4 1988 Cooperative Enterprises - Towards a Non-State Owned Industrial Organisation

Following the adoption of 1987 State Enterprise Law and then the 1988 Cooperatives Law, no amendment was made to the implicit classification of juridical persons in article 11 of the 1961 FPCivL which continued to reflect the distinction between industrial juridical persons without the right of ownership operating on the basis of civil law (ie state enterprises) on the one hand, and agricultural juridical persons with the right of cooperative-collective farm ownership operating on the basis of collective farm law (ie collective farms) on the other. Derived from the logic of that framework of analysis, cooperatives have traditionally been characterised as "different" from state enterprises. However, conceptualising the 1987 state enterprises and the 1988 cooperatives from within the participation model highlights certain connections and implications whose significance has not been previously recognised.

First, the Cooperatives Law cut across the existing classification of juridical persons based on the industry - agriculture distinction: the Cooperatives Law regulated collective farms and other agricultural cooperatives including inter-collective farm organisations,<sup>727</sup> as well as cooperatives in the industrial economy including in the sphere of production and services, and consumer cooperatives.<sup>728</sup> As such, the Cooperatives Law was the first time in Soviet history that a single law regulated juridical persons in *both* the industrial and agrarian economy.

Secondly, the Cooperatives Law was the first time that juridical persons in both the industrial and agrarian economies were regulated on the basis of a *unified* set of principles; and as such it cut across the civil law - collective farm law distinction, as well as the inherent assumption that industrial organisations did not have the right of ownership but agrarian organisations did. Principles that previously had only been applied to the agrarian economy and collective farms directly were introduced into the mainstream of the industrial economy.<sup>729</sup>

The participation model also most readily illustrates that the 1988 cooperatives, although developed from the legacy of collective farm law, were in fact based on a new form of organisation where the principal place was reserved for the participant. The members of the

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<sup>727</sup> The list of possible types of cooperative activity in the agricultural sphere were set out in article 33(5) of the Cooperatives Law.

<sup>728</sup> The list of possible types of cooperative activity in the industrial sphere were set out in article 3(2) of the Cooperatives Law.

<sup>729</sup> While remnants of the industrial cooperatives of the 1920s survived on a discrete scale in the industrial economy of the early 1980s, mainly to effect self-help joint activity of the members, they were never intended to be anything more than a small scale adjunct to the principal status of the state enterprises and associations. On the existing types of cooperative in 1985, see *supra* Section 6.1.3.



cooperatives (the participants) were at the same time the notional owners,<sup>730</sup> the managers and the workers. Participation again embodied the three basic pillars of incentivisation through self-financing; democracy in the taking of management decisions; and the importance of coercive law for the protection of the state's interests.

The underlying structure of the participation model therefore enables a comparison to be drawn with 1987 state enterprises and highlights the theoretical links between these organisations. For while they had different ownership regimes, the participation model shows that the first step away from the confirmation model came in 1987 and not in 1988; and that the core structure of the 1987 state enterprises remained as the basis for the law of all the "new" industrial Soviet organisations to 1990.

The 1987 state enterprises were the first and hence most rudimentary expression of this model. The State Enterprise Law crucially identified an interest separate from the state (ie the labour collective or worker) and then gave expression to that interest via the twin pillars of incentivisation and democratisation. The interests of the state were protected by coercive law as well as by retaining the traditional confirmation governance regime intact.

The 1988 cooperatives radicalised this structure principally due to their distinctive "characteristics" inherited from collective farm law. As a result of these new characteristics, each of the elements of the governance regime of the confirmation model became compromised in this second expression of the participation model and were reconstituted into an entirely new state governance regime based on a mixture of legal, administrative and procedural obligations.

The first distinguishing characteristic of this second expression of the participation model was that, unlike the 1987 state enterprise, the cooperatives were not created by, or explicitly owned by, the state. As such the state lost the element of "creator-owner" from the confirmation governance regime. The state could therefore no longer create or terminate all industrial organisations by diktat, nor could it just draft the purpose clause in the charter (which would limit the scope of activities due to the law of *vires*). Despite the fact that the state had lost the naked power to control creation, it readjusted the confirmation governance regime to enable it to retain negative control over the creation of cooperatives through a concealed power cloaked by the legitimation of legality. The Cooperatives Law provided for a "new" state registration process and gave to the registering agency both the right to refuse registration (including for the reason that the charter failed to conform to legislative

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On the question of who owned the cooperatives, see *infra* Section 6.4.1.



requirements); and in addition, the right to terminate the activities of the cooperative (including for flagrant violation of legislation). Therefore, while the foundations of this element of the confirmation governance regime were removed, in common with the contract-based concession enterprises, the Soviet state still managed to retain certain control over the creation and termination processes by other means.

The second distinguishing characteristic of this second expression of the participation model was that, unlike the 1987 state enterprise (and unlike the joint enterprises), the cooperatives had the right of ownership (collective farm-cooperative ownership) and therefore were capable of owning property separately from the state. The state therefore lost the element of "property-owner" from the confirmation governance regime, and hence lost the right to impose direct restrictions on property through "designation". The origins of collective farm-cooperative ownership in the history of collective farm law suggested that this form of ownership was never intended to be transferred from the agrarian economy into the mainstream industrial economy.<sup>731</sup> In contrast with the collectivisation of agriculture and its resulting effect on the legal regime of agricultural organisations, the nationalisation of the industrial economy had never contemplated nor necessitated the concession of recognising interests other than the state, either in the law on ownership, or in the law on industrial organisations.

The result of losing the elements of creator-owner and property-owner meant that this second expression of the participation model contemplated a non-state owned organisation with the separate right to own and accumulate the means of production in the industrial economy. Therefore, the development of the cooperatives network necessarily led to the erosion of the ability of the state to run the economy as a single unit based on state ownership of all the means of production through administrative instructions implementing a general national plan. State ownership and planning were simply incompatible with the growth of a separate non-state sector within the economy owning the means of production in its own right. As such, the logic of this second expression of the participation model entailed that the third element of the confirmation governance regime, "economic sovereignty", would gradually become compromised. In the short term, only by leveraging upon its continued legal sovereignty and its control of the state owned sector of the economy, was the state able, by legislative diktat, to ensure its continued control by administrative means over the national economy as a whole and the preservation of central planning despite the growing importance of the cooperatives sector.



#### 6.4.1 *Membership, the Nature of the Ownership Interest of a Cooperative, Juridical Personality and Responsibility*

As the presence of the 1988 cooperatives became more visible in the industrial economy, the question of who, if anyone, owned them became of fundamental importance. This issue was central not just to the development of the law on industrial organisations, but also to the development of the law of juridical persons generally and ultimately the law on ownership itself.

This question had always been unresolved within the context of the mainstream law of collective farms from which the 1988 cooperatives were born.<sup>732</sup> As already discussed, the issue of the ownership of collective farms had generally been ignored, hidden beneath the framework of "membership" and the legal doctrine which still considered the collective farm as falling within the state controlled national economy and the state procurement network. This approach was unfortunately broadly replicated in the provisions of the 1988 Cooperatives Law.

Once again, the concept of "membership" was central. As one contemporary textbook explained, "membership was the fundamental organisational unity of the cooperative organisation".<sup>733</sup> Reasserting again the voluntary principle that was at the heart of collective farm law, article 5 of the Cooperatives Law defined the "socialist cooperative" as "a social organisation of citizens of the USSR voluntarily associating on the basis of membership", and article 10 affirmed "the principle of voluntariness of entry into the cooperative and unhindered withdrawal therefrom."

There were general rules relating to eligibility to become a member, including for citizens, a minimum age of 16, the expression of a desire to become a member, and the capacity to carry out the purposes and tasks of the cooperative.

Although the Cooperatives Law generally used the word "citizens" when referring to the members,<sup>734</sup> article 12 provided that "in instances provided for by the present law or charter

<sup>731</sup> On the origins of collective farm-cooperative ownership, see *supra* Sections 2.3.2, 2.4 and *infra* Section 6.4.4.2.

<sup>732</sup> See *supra* Section 2.4.2.

<sup>733</sup> *Supra* n.41 (1986), p.149.

<sup>734</sup> For example, article 5 referred to an "organisation of citizens of the USSR"; article 11(1) referred to a cooperative "organised at the wish of citizens" with a minimum of three "individuals" ("*chelovek*") (the word "*chlelovek*" means a natural person/individual and can be contrasted with the word "*litso*" meaning "person" which includes both natural persons and juridical persons); and article 11(2) referred to a "general meeting of citizens".



of the cooperative, other cooperatives, state and social enterprises and organisations may also be collective members". Therefore, despite the many references specifically to citizens as members, it was clear that juridical persons could become "collective members" of a cooperative. This was a departure from collective farm law which only permitted citizens to be members of collective farms, a measure in part designed to break up the cohesion of the pre-revolutionary *dvory*.

The development of membership based on natural *and* juridical persons was yet another step towards conceiving of the Soviet economy as based upon a multiplicity of actors, other than the state, each with the right of ownership. However, as in the case of the collective farm, it was uncertain whether accession to a cooperative as a member carried with it the right to own an ownership interest of the cooperative itself. While the concept of ownership *by* the cooperative itself was a feature of mainstream Soviet civil and collective farm law,<sup>735</sup> as mentioned above, the question of who owned the cooperative, or the collective farm, was never explicitly posed and was traditionally finessed within the legal treatment of the incidents of "membership".

Membership in a cooperative carried with it the right to receive a share of the profits and the right to manage its operations through a democratic process,<sup>736</sup> and therefore might have been construed as carrying with it the additional right of ownership *of* the cooperative. However, as in the case of the collective farm, this conclusion was problematic for a number of reasons:

First there were no explicit references in the Cooperatives Law to members having ownership interests of the cooperative, despite the fact that a membership fee was contemplated. Secondly, the Cooperatives Law included the concept of a stockholder, in addition to that of a member, and this further precluded the possibility of a straightforward analysis of the issue. Thirdly, there was no concept of different sizes of ownership interest as between different members, or the accumulation of rights through the accumulation of ownership interests: members did have the right to vote and sometimes the right to be paid a liquidation dividend *but not in proportion to* the amount of the membership fee paid or any specific interest that was acquired. The level of profit distribution was more complex and was, in part only, dependent upon the amount of the fee paid. Finally, a member could be expelled from the cooperative by a decision of the general meeting which would have been problematic if the member had an ownership interest, as this would have entailed a deprivation of ownership.

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<sup>735</sup> On collective farm-cooperative ownership, see *supra* Section 2.3.2 and *infra* Section 6.4.4.2.

<sup>736</sup> These two pillars of the participation model in the context of cooperatives are considered in more detail respectively *infra* Section 6.4.2 and Section 6.4.3.



***Fees, Contributions, Funds and Withdrawal*** The law relating to entry and other fees, labour contributions and funds arguably went to the heart of the question of whether members had an ownership interest of the cooperative. Like the existence of the share fund ("*paevoi fond*") in the early collective farms, the terminology and the fact that a fee was paid, or property passed over, "suggested" that membership resulted in the "purchase" of an ownership interest. However, upon closer analysis, this did not prove to be the case.<sup>737</sup> Unfortunately the relevant terminology was not precise, and perhaps deliberately so, because explicit recognition of ownership of a cooperative by natural and juridical persons other than the state would have compromised the principle of state ownership of the industrial economy still further.

The Cooperatives Law referred to the following general concepts and terms: fees ("*vznosov*") paid by members in cash and other material assets;<sup>738</sup> entry and share fees ("*vstupitel'nykh i paevykh vznosov*");<sup>739</sup> cash entry and share fees;<sup>740</sup> fees paid by way of property passed over ("*imushchestvennym vznosom*");<sup>741</sup> share and other fees of individual and collective members of the cooperative, other enterprises and organisations and persons working in the cooperative under a labour contract; as well as cash and other property fees of its members, enterprises, organisations and citizens.<sup>742</sup> In addition to the concept of the "fee", the Cooperatives Law also contemplated the "labour contribution" ("*trudovoi vklad*"). Rather than being a payment in cash or in kind, this was a measure of the amount of participatory work that a member undertook in the activities of the cooperative.<sup>743</sup>

The Cooperatives Law also provided specific rules for "agricultural cooperatives" and specific rules for "consumer cooperatives". The general rule was that the cooperatives had the right to determine autonomously the types, amounts and procedures for formulating and using funds and reserves.<sup>744</sup>

In relation to agricultural cooperatives specifically, the Cooperatives Law provided for the possibility of a "participatory share fund ("*dolevoi fond*") of the members of a cooperative"

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<sup>737</sup> Supra n.109, p.195. See generally supra Section 2.4.2 where it is noted that the right to a portion of the share fund of a collective farm was generally regarded only as contractual, and not *in rem*, and therefore conferred neither a property interest in the fund nor in the collective farm itself.

<sup>738</sup> Cooperatives Law, article 7(2).

<sup>739</sup> Cooperatives Law, article 14(3).

<sup>740</sup> Cooperatives Law, article 48(1).

<sup>741</sup> Cooperatives Law, article 13(1) and 14(2).

<sup>742</sup> Cooperatives Law, articles 7(2), 22(1) and 36(1).

<sup>743</sup> This was adopted directly from the 1987 State Enterprise Law, supra Section 6.3.2.

<sup>744</sup> Cooperatives Law, article 20(1). This was amended by the June 1990 Amendments which required the creation of an insurance (reserve) fund. See infra 6.4.4.3.



expressed to be funded from a portion of any annual increase in production funds. Assets were then distributed from this fund to members' "personal accounts" in proportion to their specific labour contributions. This participatory share fund therefore had nothing to do with fees paid by members but, as noted by the Cooperatives Law itself, was just a further method to incentivise work for the "improving use of production funds" and increasing labour contributions.<sup>745</sup> Although this fund was expressed to be "of the members" (and not of other employees of the cooperative) and may have been an incident of membership, it would have been difficult to have viewed it as evidence of ownership by members of an ownership interest of the cooperative itself. Indeed the waterfall of payments on the termination of an agricultural cooperative treated the claims of members in respect of this fund like other creditors.<sup>746</sup>

In relation to consumer cooperatives specifically, the Cooperatives Law stated expressly that "members...shall make cash entry and share fees", and that when a member withdrew, he was entitled to be reimbursed the amount of his share fee and a portion of distributable profits, but not his entry fee.<sup>747</sup> While the right of "unhindered withdrawal" was included for all members of all types of cooperative generally,<sup>748</sup> it seemed therefore that the right to have the share fee returned on withdrawal only applied to consumer cooperatives.

These provisions taken as a whole presented a very confused picture. In particular, the only "obligation" in the Cooperatives Law actually to pay an entry or share fee was set out in the specific rules governing consumer cooperatives (and not others forms of cooperative) although other sections of the law clearly did contemplate their existence. If fees were due, it was unclear: what exactly these different fees were for; when these fees were payable (the legislation contemplated entry and "other" fees); whether they were to be paid in cash or in kind; whether they were returnable (other than in the case of consumer cooperatives); and whether they were paid only by members or by others (the legislation contemplated fees "of members" as well as "of other enterprises and organisations and persons working in the cooperative under a labour contract").

In these circumstances, it seems that the "entry and other fees" are best regarded as fees paid in connection with membership but not as consideration for the purchase of an ownership interest. The right to withdraw further suggested that the membership was a right against the

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<sup>745</sup> Cooperatives Law, article 36(2).

<sup>746</sup> In fact these claims seem to have been preferred to those of other creditors (Cooperatives Law, article 36(3)). *Infra* Section 6.4.4.1.

<sup>747</sup> Cooperatives Law, article 48(1).

<sup>748</sup> Cooperatives Law, article 10(1).



cooperative and the other members, and did not give rise to an ownership interest that could have been sold on a withdrawal to another.

Although it is difficult to conceive of membership fees as consideration for the purchase of an ownership interest of a judicial person, there was, on the other hand, no hint in the Cooperatives Law that the law on common ownership applied to property of a cooperative, and therefore no suggestion that fees or property paid by members remained in their ownership. There was no mention of "contributions" or "participatory shares". Thus the terminology was consistent with that used for collective farms, and can be distinguished from the language of the contract for joint activity and the joint enterprise. The latter were developed from the traditional framework for industrial associations without the independent right of ownership.<sup>749</sup> The cooperatives, by contrast, were developed from the legacy of the collective farm and the framework of collective farm-cooperative ownership.

***Ownership Interests and Stocks*** Although cooperatives were clearly to be juridical persons, the Cooperatives Law was entirely silent on the question of the existence or nature of an ownership interest *of* the cooperative itself. In all the many references to the payment of fees, there was no mention that these resulted in anything other than "membership" (distinguishable from "ownership"). Even the general provisions setting out the rights of members did not include a right of members to own the cooperative itself.<sup>750</sup> It is therefore suggested that the previous analysis presented in this study with regard to the ownership of collective farms still applied in relation to the 1988 cooperatives.<sup>751</sup>

There was, however, one important difference between the prevailing collective farm law and the Cooperatives Law. In addition to the concept of "membership", the Cooperatives Law also contemplated the existence of "stocks".

"As a further source of financing", the Cooperatives Law expressly permitted the issue of stocks ("*aktsii*") for sale to (i) members; (ii) persons working at the cooperative under a labour contract; or (iii) enterprises or organisations.<sup>752</sup> In addition, the Cooperatives Law contemplated the issue of "other securities" ("*tsennye bumagi*").<sup>753</sup> While the term for "securities" in the Russian language includes both debt and equity securities, the term "stock" refers only to equity securities - ie an ownership interest of a juridical person.

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<sup>749</sup> Supra Sections 4.6 and 5.4.2.2.

<sup>750</sup> Cooperatives Law, article 13(1).

<sup>751</sup> Supra Section 2.4.2.

<sup>752</sup> Cooperatives Law, article 22(4).



In light of this basic "definitional" understanding as to the meaning of "stocks", the rules relating to the issuance of stocks by cooperatives made little sense: They provided that stocks could only be issued following a verification of solvency from a bank; stocks were expressed "to be secured" ("*obespechivayutsya*") by all the property of the cooperative; stocks were available to be purchased by members on a preferential basis; as a rule, the total value of the stocks should not have exceeded the gross revenue ("*valovogo dokhoda*") for a year. The cooperative was to establish the procedure for payment of the annual revenue on stocks ("*na aktsii godovogo dokhoda*") and that this annual revenue could not be changed other than at a general meeting of members "with the participation of stockholders".<sup>754</sup>

It is tempting to understand the reference to "stocks" as an example of inappropriate drafting. Despite the reference to the term "stocks and *other* securities" [emphasis added], this phrase was only intended to relate to debt securities. The law governing the right to vote, to receive a share of profits and to receive a portion of the residual property on the termination of activities (considered below) also suggested that the "stock" was not meant to be understood as an equity interest; or if it was, it was more like preferred stock than ordinary stock. The use of the term "annual revenue" (which suggested more of an "interest" type quality and avoided the use of the term "dividend") further bolstered the argument that "stocks" were not to be understood as equity.

However the word in the Russian language for "stock" does mean an equity interest, and as part of the June 1990 Amendments, the term "dividends on stocks" ("*dividendov po aktsiyam*") was included in article 20(1) of the Cooperatives Law which suggested that despite the reference to "annual revenue", the term "stock" really did mean an equity interest. Furthermore, civil law textbooks of the early 1990s, written after the development of joint-stock societies and a clearer understanding of the notion of the stock had been established, still, on the basis of this legislation, confirmed the right of the cooperative to issue stocks (without comment as to the implications for understanding its ownership regime).<sup>755</sup> The situation was only fully cleared up almost eight years later by article 109(3) of the 1994 Russian Civil Code (Part 1) which expressly provided that "cooperatives shall not have the right to issue stocks".

***Right to Vote and Right to Receive a Portion of Revenues (and Stocks)*** If the amount of votes a member cast or the amount of revenues a member received had been *proportionate* to

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<sup>753</sup> Cooperatives Law, article 7(2).

<sup>754</sup> Cooperatives Law, article 22(4).

<sup>755</sup> Supra n.412, p.243: "Authorisation to issue stocks is given to a cooperative".



the amount of the membership or other fee paid by that member then this may have been evidence of the existence of an ownership interest. However this was not the case. The Cooperatives Law provided that "each member...shall have one vote *irrespective of the amount of its fee* paid in property ("*razmer ego imushchestvennogo vznosa*")";<sup>756</sup> and that "members...shall have the right to...receive a share of the revenue (profit) subject to distribution among members...*in accordance with labour contribution*, and in the instances provided for in the charter, also in accordance with the fee paid in property to the cooperative".<sup>757</sup> Both of these regimes were consistent with the interpretation of the member as a participant in the activities of the cooperative contributing with personal labour efforts, but did not suggest that they were the owners of the cooperative. Furthermore, stockholders (in their sole capacity as stockholders) were not generally given the right to vote or the right to receive a portion of revenues (in addition to the fixed "annual revenue") which further suggested that stocks were intended to have the character of debt or preferred stock.

***Right to Receive Residual Property on Termination (and Stocks)*** The initial redaction of the Cooperatives Law provided the general rule that "property, remaining after the liquidation of a cooperative, shall be used in the procedure established by civil legislation if not otherwise provided in this Law".<sup>758</sup> This merely avoided the direct issue of whether a member had a residual right in the liquidated assets. The situation was clarified following the June 1990 Amendments which amended this general provision to read that: "when liquidating a cooperative, the property left after accounts with the budget, banks and other creditors shall be distributed between members of the cooperative". However, there were additional provisions on liquidation relating specifically to each of the agricultural cooperatives, production cooperatives, and consumer cooperatives.

For the agricultural cooperatives, the initial redaction of the Cooperatives Law provided that after settling accounts with regard to the payment of labour, payments of personal accounts of members, assets from the participatory share fund, and fulfilment of obligations to the budget, banks, stockholders and other creditors, the distribution of any residual amounts shall be determined by the board of the collective farm for the benefit of other collective farms in agricultural production.<sup>759</sup> This further suggested that membership did not entail an ownership interest (at least in the context of agricultural cooperatives), as members of agricultural

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<sup>756</sup> Cooperatives Law, article 14(2) [emphasis added].

<sup>757</sup> Cooperatives Law, article 13(1) [emphasis added]. The procedure was decided by the general meeting (see Cooperatives Law, articles 14(3) and 20(1) see also 25(2)).

<sup>758</sup> Cooperatives Law, article 15(3).

<sup>759</sup> Cooperatives Law, article 36(3).



cooperatives were not entitled to any residual property upon liquidation. Furthermore, it seemed that stockholders were treated like creditors and this reinforced the interpretation that the reference to stock was intended only to be understood as a debt security. These provisions changed following the June 1990 Amendments which provided that the final residual property should be distributed among members and not given to other collective farms.

For the production cooperatives, the initial redaction of the Cooperatives Law provided that residual property after the payment of labour wages, and fulfilling obligations to the budget, banks and other creditors, shall be distributed among members "in the procedure and on the conditions provided for in the charter".<sup>760</sup> Although stockholders were not specifically mentioned, the rules for production cooperatives did provide members clearly with a potential right to residual property. The June 1990 Amendments merely deleted the phrase relating to the method of distribution being set out in the charter.

For the consumer cooperatives, yet another rule applied. The provisions followed a similar description of deductions as for the production cooperatives, but the final residual property was expressed to be distributed, not to the members, but to the cooperatives union (or association) of which the consumer society was a member.<sup>761</sup> This was unamended by the June 1990 Amendments.

These rules were therefore different for different types of cooperative and changed over time from a situation where members did not have an explicit right to a share in the residual assets to one where members (other than in consumer cooperatives) were given this right. Unless the view is taken that different types of cooperative had different types of ownership interest (if at all), the termination regimes were by no means conclusive evidence of the presence of "an ownership interest" of members.

***Right of Expulsion*** There were only a few brief references to the right of expulsion in the Cooperatives Law. They contemplated the right of the general meeting to "expel" a member from the cooperative in the instances provided for in the charter.<sup>762</sup> While the right to expel a member did address the question of the ownership interest directly, the language of "expulsion" is more suitable to the status of membership based on contract than upon ownership of an ownership interest of a juridical person. The right to deprive a member of an ownership interest would have been subject to the general law on ownership and provisions relating to the deprivation of the right of ownership. If expulsion amounted to the deprivation

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<sup>760</sup> Cooperatives Law, article 44.

<sup>761</sup> Cooperatives Law, article 45(5).

<sup>762</sup> Cooperatives Law, articles 11(2), 12(4) and 14(3).



of an ownership interest, then more detailed rules on expulsion and the deprivation of property would have been expected to have been included in the Cooperatives Law, rather than leaving the matter to be regulated by the provisions of the charter and general meeting.<sup>763</sup>

***Summary and Autonomous Property Responsibility*** From the above it is abundantly clear that there was no clear understanding of what "an ownership interest of a cooperative" actually meant as a legal matter or whether it existed at all. This lack of clarity on such a central doctrinal issue was probably in part due to the legacy of state enterprises (which had no ownership interests as they were conceived of as indivisible objects of state ownership without the separate right of ownership) and the law of collective farms (which did not clearly address the question and finessed the point beneath discussions on the doctrine on membership).

On the basis of the positive law, it is difficult to come to a sensible interpretation on the ownership interest question in the context of the 1988 cooperatives. It seems that the strict legal position was that although the state and members had various rights as against the cooperative, neither the state nor the members "owned" the cooperatives and furthermore, stockholders only acquired an interest as a creditor against the cooperative. The cooperatives regime therefore operated by virtue of the state's position, not as owner, but as legal sovereign and through statute which provided a legal framework for circumstances where the nature of the ownership interest (and the specific rights and obligations attached to it) would otherwise have regulated the matter (eg on termination, distribution of profits, responsibility etc).

The effect of the uncertain ownership position was reflected in the rules relating to the autonomous property responsibility of the cooperatives. The responsibility rule for any juridical person is usually drafted on the basis of separating responsibility of the legal owner from that of the juridical person. While the labour collective had a significant role in the activities of the 1987 state enterprises, they were clearly not the legal owners, and as such, article 2(6) of the State Enterprise Law separated the responsibility of the state only (ie the legal owner) from that of the state enterprise (presumably on the basis that there could be no question of liability falling on the labour collective even though it was referred to as the "proprietor").<sup>764</sup> By contrast, article 8(4) of the Cooperatives Law provided that *both* the state *and* the members shall not be responsible for the debts of the cooperative. This further evidenced the fact that the ownership regime of the cooperatives was unclear (or even absent)

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<sup>763</sup> The importance of deprivation of property rights was noted in Cooperatives Law, article 8(1) which provided that property of a cooperative could only be withdrawn by a decision of a court or arbitrazh.

<sup>764</sup> On the meaning of the term "proprietor" in this context, supra Section 6.3.4.3.



and that in these circumstances it might have been inferred that either the state *or* the members could have been responsible for the debts of the cooperatives, and consequentially the Cooperatives Law referred to both in separating responsibility.

Article 8(4) had two additional features: it provided that, in certain specific circumstances, members could have been made to be responsible for debts of certain cooperatives; and that the "basic assets" of the cooperative were available for execution by creditors.

In the case of production cooperatives only, the members were expressed to bear subsidiary responsibility for debts of the cooperative "in the procedures, amounts, and conditions provided for in the charter".<sup>765</sup> The June 1990 Amendments introduced a minimum level of responsibility to be no less than the annual revenue received by the member; and amended article 11(4) to require all charters of production cooperatives to include provisions for the level of responsibility of members for debts of the cooperative (or else registration would be refused). The nature of the liability of an owner of an ownership interest in a juridical person would generally be regulated by the rights and obligations attached to the particular ownership interest. Thus, for example, a stockholder in an English "plc" has limited liability (a characteristic of being an owner of stock). As the cooperatives did not have a specific ownership interest (or as the question was overlooked), the state "had to" provide through the legal system a default regime for responsibility. This was achieved in the case of the production cooperative by the Cooperatives Law specifying that the nature and level of responsibility was a matter that had to be set out in the charter.

The inclusion of "basic assets" of the cooperative within its property responsibility (and hence the assets available to creditors) was significant because it amended the underlying civil law position which applied to the confirmation enterprises and which excluded most basic assets of an industrial juridical person from the property available to creditors.<sup>766</sup> This expansion in the scope of responsibility again signalled the development towards a concept of liability (rather than responsibility) understood in terms of the position at liquidation. The first expression of the participation model had introduced financial indicators into the liquidation procedure. The second expression, the Cooperatives Law, developed this further,<sup>767</sup> suggesting that a regime of limited liability may have been just a short step away.

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<sup>765</sup> Cooperatives Law, article 43.

<sup>766</sup> Supra n.270. This change was pre-empted by the responsibility rules that applied to the contract-based concession enterprises (supra Section 5.3.2).

<sup>767</sup> On termination rules, infra Section 6.4.4.1.



#### 6.4.2 *Participation and Incentivisation - the First Pillar*

"Participation" entailed personal involvement and interestedness in the activities of the cooperative, in the distribution of revenues and in the decision making process.

In the case of the cooperatives, participation took two forms: In production cooperatives, membership was conditioned upon obligatory "personal labour participation" in the production activities.<sup>768</sup> In consumer cooperatives, while personal labour participation was not prohibited and while members had preferential rights to work in the cooperative system, the concept of participation emphasised to a greater extent an involvement in the orientation of the activities of the cooperative to ensure that production satisfied the needs of its members.<sup>769</sup>

This concept of the participant as active in the business of the enterprise/cooperative broadly precluded the development of the concept of the "silent member" acting as an equity investor, where a payment or fee is made, not with a view to participating in the activities of the cooperative, but with the aim of acquiring an ownership interest of the cooperative in order to realise a return linked to profits and upon a sale of that interest. In contrast to the participant, a stockholder may have had such an opportunity. However, as discussed above, the notion of "stocks" was not sufficiently developed in the legislation to lead to the conclusion that stocks were intended to represent equity capital. The participation enterprises thus in traditional terminology were conceived broadly as an association of persons (rather than of capital) where members had the right and obligation to "participate" personally in its activities. For this reason, not only is this model indebted to collective farm legislation, but also to the "bridge", the contract for *joint activity*. In line with this analysis, while the legislation contemplated the hire of non-members pursuant to a labour contract, the Cooperatives Law provided that the "state shall take measures to prevent instances of the use of cooperatives for private entrepreneurial activities with the use of hired labour in the guise of creating

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<sup>768</sup> Cooperatives Law, articles 3(2) and 40(2). This is more akin to the type of participation in the first expression of this model. The participants of the first expression of this model were workers and therefore participated in the activities of the enterprise almost by definition. Yet the State Enterprise Law, adopting the technique of coercive law, still provided that "it is the debt of each worker to labour honestly and conscientiously, to increase labour productivity, to improve the quality of products, to take care of and augment the national good and comply with labour discipline" (State Enterprise Law, article 14(1)).

<sup>769</sup> The Cooperatives Law provided that "membership in a consumer society shall not be conditioned by the labour participation of citizens in its activity" (article 48(1)). However the principal task of a consumer cooperative was "to guarantee the provision of goods, services and work to its members" and members had the "right of preferential acquisition of goods in cooperative stores...and also a preferential right to receive work in the consumer cooperative system" (Cooperatives Law, articles 45(3) and (4)).



cooperatives."<sup>770</sup> This limitation attempted therefore to ensure that the practice of hiring workers did not compromise the personal participation principle of members.

Like the first expression of this model, the obligation to participate was intended to be "incentivised" through "broad opportunities" for "the receipt of revenues dependent upon the quantity and quality of [their] labour".<sup>771</sup> It was hoped that production efficiencies would result from creating a "material interest" of the members in the profitability of the cooperative.<sup>772</sup> In short, this first pillar as applied in the second expression of the participation model comprised the application of the "new economic principles" coupled with the right of a member to share in the profits divided *prima facie* in accordance with labour contributions.

The new economic principles of the 1987 state enterprises were developed further in the Cooperatives Law. While providing for operation on the basis of "self-financing",<sup>773</sup> "nonsubsidy",<sup>774</sup> and in the case of production cooperatives, full *khozraschet*, the Cooperatives Law also required that their activities be conducted on the basis of "the principles of socialist economic operations and...the extensive use of goods-money relations".<sup>775</sup> The incorporation of "socialist economic principles" provided the basis for state mandatory rules governing the operations of the cooperatives, and the use of "goods-money relations" indicated the developing use of civil law contractual relations. Both of these aspects are considered later in this Chapter.<sup>776</sup>

In common with the first expression of this model, the principles of self-financing and nonsubsidy were aimed at ensuring that the cooperative operated autonomously and was not required to subsidise other cooperatives. But again like the first expression of this model,<sup>777</sup> there were instances where the Cooperatives Law contemplated the "rendering of financial support" by the state "including on conditions of the assets being reimbursed".<sup>778</sup>

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<sup>770</sup> Cooperatives Law, article 40(2).

<sup>771</sup> Cooperatives Law, article 1(1).

<sup>772</sup> Cooperatives Law, articles 1(5) and 5(1).

<sup>773</sup> Cooperatives Law, article 17(1).

<sup>774</sup> Cooperatives Law, article 20(1), because "loss-making work is incompatible with the essence thereof".

<sup>775</sup> Cooperatives Law, article 17(1).

<sup>776</sup> *Infra* Sections 6.4.4.3 and 6.5.

<sup>777</sup> *Supra* n.678.

<sup>778</sup> Cooperatives Law, article 22(2). The reference to "reimbursement" ensured as a legal matter that any state aid was characterised as a loan, and not as a subsidy or grant.



The distribution of gross revenue was "the exclusive right of the general meeting of members",<sup>779</sup> and was to be based "in accordance with labour contribution, and in the instances provided for in the charter, also in accordance with the fee paid in property to the cooperative".<sup>780</sup> This aspect of the Cooperatives Law was inherited from one of the key features of collective farm law and the 1987 state enterprises (ie payment in proportion to work). The right to provide for an alternative distribution mechanism in accordance with property fees paid was an exception to the general participation model rule. It can be understood in terms of the way in which this expression of the model, while rooted in the three basic pillars, was also searching forward towards an organisational form based on stocks, equity capital and dividends, but was unable to reach to that position, in part due to a tension between such a position and the participation principle, and in part due to an incomplete understanding of certain of the basic principles, most importantly the nature of the ownership interest.

#### 6.4.3 *Participation and Democracy - the Second Pillar*

While the first expression of this model pioneered the departure in the industrial economy from the one-man management/one interest framework, the cooperatives, embracing their collective farm heritage, further developed the principle of participant democracy.<sup>781</sup> The Cooperatives Law provided generally that "the administration of a cooperative shall be carried out on the basis of socialist self-management, broad democracy, *glasnost* and active participation of its members in deciding all questions of activity of the cooperative."<sup>782</sup>

In this second expression, the removal of the state from its role as creator-owner and hence from the internal democracy of the enterprise, enabled an internal management democratic framework to be developed on the basis of the voting mechanism between members. The Cooperatives Law called this "socialist self-management". While the state was indeed no longer an owner, the reference to "socialist" was no doubt left as a marker that there were limits to the choices that members could make and that their decisions had to be adopted

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<sup>779</sup> Cooperatives Law, articles 14(3) and 20(1).

<sup>780</sup> Cooperatives Law, article 13(1).

<sup>781</sup> The traditional division between the confirmation state enterprise and the collective farm was noted in the "Handbook for the Chairman of a Collective Farm" which stressed that "state enterprises [are] where all the means of production and produced products belong to the state...[and] are administered on the basis of one-man management by the director having a power of attorney to administer on behalf of a state agency. In collective farms, as a voluntary production cooperative association, where social ownership of the means of production is the basis thereof, the labour collective manages directly on the basis of a broad democratic foundation". (*Spravochnik Predsedatelya Kolkhoza - Kniga Pervaya* (Gosudarstvennoe Izdatel'stvo Sel'skokhozyaistvennoi Literatury:1956), p.172).

<sup>782</sup> Cooperatives Law, article 14(1).



taking into account the general "interests" of socialism. This broad implicit restraint on the internal decision making process was borrowed from the concept of collective farm democracy where the state was also excluded from direct management.<sup>783</sup>

As the participation model was based on the personal participation of the members in management, and in the absence of a formal separation of ownership from control, its governance regime was centred more around balancing the interests of members *inter se* rather than aligning the interests of the member (or owners) with those of the managers. The Cooperatives Law explicitly provided that "disputes relating to cases arising from membership relations" shall be settled by the organs of the cooperative as set out in the charter, and in instances provided for by legislation, a court.<sup>784</sup>

The principal organ and forum for the resolution of differences between members and for deciding upon policy was the general meeting. Its expressed purpose was to "direct current affairs" of the cooperative.<sup>785</sup> Each member had one vote irrespective of the fee paid, and the workers who were not members had a consultative vote. The general meeting had exclusive competences in key areas, including adopting the charter and changes thereto; electing the chairman, (in the case of large cooperatives) a board, and an audit commission; determining amounts of entry and share fees; establishing a procedure for the distribution of revenues (profits) and for the creation of internal funds; deciding questions relating to withdrawal and expulsion of members and the termination and reorganisation of the cooperative. Other areas of competence were permitted to be specified additionally in the charter.

Residual authority and general "guidance over current affairs" was relegated to the chairman (or the board, in the case of larger cooperatives).<sup>786</sup> Additionally the chairman was responsible for ensuring that the decisions of the general meeting, and if applicable, the board, were carried out. The audit commission (or single auditor) verified financial and economic activities.

The most noticeable feature of the provisions of the Cooperatives Law relating to the internal organs and procedures was their brevity. This continued the tradition set out both in the State Enterprise Law, collective farm legislation and the contract-based concession model. Despite providing for three internal organs and a chairman, there was only one article in the

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<sup>783</sup> See supra Section 2.4.1. The nature of the state control over the management process by external and legislative constraints on members is examined infra Section 6.4.4.

<sup>784</sup> Cooperatives Law, article 12(3).

<sup>785</sup> Cooperatives Law, article 14(2).

<sup>786</sup> Cooperatives Law, article 14(4).



Cooperatives Law related specifically to their operation and constitution. No default rules were provided relating to the calling of meetings, information requirements to be circulated prior to meetings, quorum requirements, majority and supra-majority voting, method of voting (secret or open), and the procedures in the event of deadlock etc. All of these areas were left to be elaborated in the charter, or to be decided upon by the general meeting itself. There seemed to be no appreciation of the fine balance to be struck in legislation on enterprises between procedural, mandatory and default rules. Although the cooperative enterprise was an independent industrial organisation, the brevity of the legislation almost suggested that it was still owned by a single owner and still governed by a one-man manager, and hence there was no need to provide for an elaborate internal governance framework.

As in the contract-based concession model, now that the state had been excluded from the internal management organs of the cooperative, legislators seemed to be more interested in ensuring that the state's interests were protected than in developing rules relating to internal organs. Therefore, by contrast with the provisions relating to the internal organs, the Cooperatives Law contained 12 articles on the "Economic Principles of Economic Machinery in System of Cooperatives" (ie economic relations with the state) and a further 4 articles on "The State and the Cooperative" (ie state aid and political relations). Clearly explicit detailed legal regulation of relations with the state was critical because in this second expression of the participation model each of the distinctly Soviet elements of the governance regime of the confirmation model had been dismantled: the state was no longer the creator of the cooperatives, nor the owner of their property, nor therefore the sole owner of the industrial economy. A new governance regime therefore had to be constructed to ensure that the cooperative, like the collective farm, operated by way of "combining" personal and collective interests with those of the state.<sup>787</sup>

#### 6.4.4 *Protection of the Interests of the State*

Both of the first two pillars of the participation model as applied to cooperatives had a "socialist" dimension to their operation, and hence the Cooperatives Law referred to "the principles of socialist economic operations" and "socialist self management". Like the state regulation of the collective farm, there was no intention that exclusion of the state from the organisation as an owner would entail a loss of control by the state over its activities. In relation to each element of the confirmation governance regime that had been lost in this

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<sup>787</sup> Cooperatives Law, article 10(1). This was also (co-incidentally?) the same list as the new forms of ownership that were to be adopted pursuant to the 1990 Ownership Law, see *infra* Section 7.3.



second expression of the participation model, the state therefore adjusted its position in order to ensure that its interests continued to be protected.

#### 6.4.4.1 *Loss of Role as Creator-owner*

As distinct from the first expression of this model, cooperatives were created by the participants and not by the state. Article 11 provided that cooperatives were organised at the will of citizens on a voluntary basis. The charter of the cooperative was adopted by the general meeting of citizens and the cooperative was deemed to be formed upon registration of the charter. There had to be at least three individual members.

It seemed therefore that the state had lost its right to protect its interests through the first element of the governance regime of the confirmation model - acting as state-creator. In the confirmation model, the state used its position as creator to determine when to create all industrial organisations, to specify the purpose clause of the charter (and hence rely on the *vires* rules to ensure compliance with the purpose) and to terminate its activities.<sup>788</sup>

Despite the loss of its status as creator in this second expression of the participation model, the state developed an alternative "indirect" regime for retaining negative control over the creation of cooperatives (hence control over the contents of the purpose clause of the charter) through the right to refuse registration; and positive control over the termination of activities, through the guise of ensuring financial stability and compliance with law.

Article 11(1) in the initial redaction of the Cooperatives Law set out (rather misleadingly) the general principle that "the creation of a cooperative shall not be conditional upon any special authorisation of soviet, economic or other agency". Article 11(4) however seemed to provide an exception: "the executive committee of the regional, district, city, district within a city soviet of people's deputies shall have the right to refuse to register the charter of a cooperative only in the instances of it being contrary to prevailing legislation". Any refusal to register was appealable to the registering agency.

This registration regime clearly fell short of an "incorporation model" where members have the right to incorporate a judicial person and have their organisation registered provided that all "formal" registration documents are duly presented (irrespective of content). By contrast, under the article 11 procedure, first, the registration body was an agency of the state; secondly, it was given broad discretion to refuse to register charters on non-procedural grounds; and thirdly, it (rather than an independent tribunal) had the right to hear appeals.

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See supra Sections 3.2 and 3.4.1.



The June 1990 Amendments acknowledged the reality of this situation and deleted the reference in article 11(1) to the fact that registration was not conditional upon any authorisation. It also introduced references to a licensing regime for certain activities thereby extending the ambit of state control.<sup>789</sup> In addition, the June 1990 Amendments seemed to expand the circumstances where registration could have been refused,<sup>790</sup> but did however provide for judicial determination of any appeals and made it clear that registration could not have been refused for reasons of inadvisability.

Each charter was still required to contain a purpose clause,<sup>791</sup> and control over the formulation of this clause was important for two reasons: first the civil law *vires* rules prohibited any activities contrary to this purpose;<sup>792</sup> and secondly, the law on collective farm-cooperative ownership only permitted the ownership of property necessary to carry out the specified charter tasks.<sup>793</sup> Although formally registration agencies were not permitted to refuse registration for reasons of inadvisability, control over the registration process meant that the charter purposes could have been scrutinised and might either have been subject generally to a licensing requirement or, if perceived as contrary to the state's interests, the registration of the charter in practice could have been delayed or refused.

As such, while the state was no longer the creator of these industrial organisations, and while until June 1990 their creation was expressed to be without the need for authorisation, the state did in fact retain negative control over the registration process: ie the right in practice to delay or veto an application. The state's discretion moved from a "naked" power (such as in the

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<sup>789</sup> Cooperatives Law, articles 3(1) and 17(2) (as amended).

<sup>790</sup> Registration could have been refused where there was "a violation of the established procedure for the creation of a cooperative, when its charter fails to conform to the requirements of legislation, and also if responsibility of members of the cooperative for the debts of the cooperative has not been provided for in the charter [of production cooperatives]...A refusal to register a cooperative for reasons of inadvisability shall not be permitted" (Cooperatives Law, article 11(4), as amended).

<sup>791</sup> Cooperatives Law, article 11(2).

<sup>792</sup> On the civil law of *vires*, see supra Section 3.4.1. Article 3(1) of the Cooperatives Law permitted the inclusion in the charter of any type of activity not prohibited by legislative acts and the preamble noted that cooperatives had the right of "a free choice of form of economic activity". Article 5(3) then provided that the cooperative had "the right to adopt any decisions if this is not contrary to prevailing legislation and the charter". Like the equivalent provisions of the first expression of this model (supra n.694), this formulation indicated that the special legal capacity authorisation regime was developing into a more permissive regime (infra n.922).

However the June 1990 Amendments reasserted again the more authoritarian regime by supplementing article 17(2) to specifying that: "a cooperative shall not have the right to carry out any activity which does not correspond to the subject and purposes provided by its charter, and in instances established by legislation, - and by issued licences". The regime of special legal capacity was reinforced by the practice of listing the "rights" of the cooperatives in the Cooperatives Law (see article 8(3)).

<sup>793</sup> See infra Section 6.4.4.2.



confirmation model, and in the contract-based concession model where creation was entirely at the behest of the state) to a power cloaked by the legitimation of law. This power to refuse to register charters was presented both in terms of a licensing regime and a right to monitor content with the professed aim of ensuring that all charters conformed to legislative requirements. In practice this system was clearly open to abuse, and while more progressive than the concession model, it did not even nearly resemble a right to incorporate.

Despite the state's lack of ownership of cooperatives or their property, the technique of maintaining negative control over the creation of cooperatives, through characterising the role of the registering agency as the guardian of legality, was also applied in the context of the termination procedures.

In common with the regime of the first expression of this model, termination was expressed to occur by way of reorganisation (merger, accession, separation, division or transformation) or termination/liquidation.<sup>794</sup> This again included the possibility for a transformation. Liquidation could occur as a result of a decision of the general meeting *or* of the executive committee of a local soviet of peoples deputies which registered the cooperative.

The local soviet was given the right to liquidate the cooperative if the cooperative was "trading at a loss (*"ubytochnosti"*) and was insolvent (*"neplatezhеспособности"*) and in the instances when the cooperative, irrespective of a rendered warning, repeatedly or flagrantly violates legislation".<sup>795</sup> Members had the right to appeal a decision by a local soviet to liquidate it. Initially this appeal was to the local soviet itself, but after the June 1990 Amendments, appeals were considered by courts.<sup>796</sup> In addition, following a similar right in the first expression of this model, the initial redaction of the Cooperatives Law also provided that a cooperative that had systematically breached its credit obligations may be declared by its bank to be insolvent. Thereafter, if the cooperative was trading at a loss, the bank was given the right to request the relevant local soviet to commence liquidation proceedings against the cooperative with a view to protecting the property interests of creditors.<sup>797</sup>

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<sup>794</sup> Cooperatives Law, article 15. See *supra* Section 6.3.4.2.

<sup>795</sup> Cooperatives Law, article 15(2). The June 1990 Amendments provided for a test based only on insolvency for more than six months.

<sup>796</sup> Cooperatives Law, article 15(2).

<sup>797</sup> Cooperatives Law, article 23(3) and *supra* n.713. Following the June 1990 Amendments, insolvency could only have been declared by a bank if a cooperative failed to fulfil its obligations with regard to its accounts; and if it was insolvent for more than six months, a bank then had the right to request liquidation proceedings by the local soviet.



As with the first expression, the movement to termination provisions based on protection of creditors and financial stability suggested a reconceptualisation of the industrial organisation as a creature of a market economy and hastened the development of a regime of limited liability. However, by making the registering agency, rather than actual creditors, the guardian of legality and solvency, again the Soviet state retained influence in a process which it could no longer control by direct means (having lost its role as creator of all industrial organisations).

#### 6.4.4.2 *Loss of Role as Property-owner (Cooperative Ownership)*

As distinct from the first expression of this model, the cooperatives had the right to own property in their own right, by way of "collective farm-cooperative ownership". The Stalin Constitution had originally conceived of "socialist ownership of the USSR" comprising "state ownership" and "cooperative-collective farm ownership". As has been described already, the Cooperatives Law cut across the traditional distinctions implicit in the then existing classification of Soviet juridical persons between juridical persons operating in the industrial economy without the right of ownership on the basis of civil law, and those different juridical persons operating in the agrarian economy with the right of ownership on the basis of collective farm law.

The radical step taken by the Cooperatives Law was to introduce the collective farm/agricultural economic settlement into the industrial economy, thereby granting to the 1988 *industrial* cooperatives the right of ownership which had been won by collective farmers in the context of the collectivisation settlement of the 1930s and which applied at that time primarily only to agricultural collective farms.<sup>798</sup> Unwilling to explore the consequences of providing for a single framework for an industrial and agrarian juridical person with the right of ownership, the Cooperatives Law continued to characterise the national economy as based on the separate forms of state (all-people's) ownership and collective farm-cooperative ownership.<sup>799</sup> However, after 1988 this distinction simply became less "relevant" as it no longer formed the basis for distinguishing industrial from agrarian juridical persons, and civil law from collective farm law.

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<sup>798</sup> On the historical origins of the collective farm-cooperative ownership, *supra* n.41 (1982), p.258.

<sup>799</sup> "The leading role of state (all-people's) form of ownership [and] the cooperative form is developing everywhere" and that "cooperative enterprises...together with state enterprises (associations) shall be the basic link of the unified national economic complex" (Cooperatives Law, articles 1(2) and 1(4); see also *supra* n.610). Note that the Brezhnev Constitution referred to "collective farm-cooperative ownership" (article 10) rather than to "cooperative-collective farm ownership" as set out in the Stalin Constitution.



Under the general law of collective farm-cooperative ownership, cooperatives had the right to possess, use and dispose of property in their ownership as established by their charters, but only to the extent that such property was "necessary for the carrying out of charter tasks".<sup>800</sup> The Cooperatives Law developed this position by providing that only property "necessary for carrying out charter tasks...and...in accordance with the purposes of its activities" could be in their ownership,<sup>801</sup> and affirmed the principle that the right of disposition only belonged to the cooperative itself.<sup>802</sup> Using the same term that the State Enterprise Law had used to describe the labour collective, the Cooperatives Law described the cooperative as the "fully fledged proprietor" of the property belonging to it by right of ownership.<sup>803</sup> It is unclear what this terminology added, but it did serve to illustrate the continuous thread through the first two expressions of the participation model.

The significance of the provisions of the Cooperatives Law on collective farm-cooperative ownership was principally threefold.

First, the Cooperatives Law no longer referred to "collective farm-cooperative ownership" but only to "cooperative ownership".<sup>804</sup> This may have not been noticed at the time, however this shift in expressions evidenced the beginnings of the reformulation of the terminology of the Stalin ownership regime.<sup>805</sup> Secondly, it provided that cooperative ownership "as a form of socialist ownership shall be inviolable and under the protection of the State. It shall be protected by law equally with state ownership".<sup>806</sup> The state was then directed "to facilitate in every possible way the development of cooperative ownership".<sup>807</sup> This therefore gave it an equal status to state ownership and evidenced a "coming together" of two distinct forms of ownership, illustrating a possible shift towards a generic concept of ownership applied to all

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<sup>800</sup> 1961 FPCivL, article 23. The rules governing collective farm-cooperative ownership were set out in the Brezhnev Constitution, article 10, the 1961 FPCivL, articles 20 and 23; and civil codes, for example, RSFSR CC, articles 99-101.

<sup>801</sup> Cooperatives Law, article 7(1). This article also included a list of property that could be owned subject to the conditions set out above. Clearly, property designated exclusively within the ownership of the state would be excluded (1961 FPCivL, article 21).

<sup>802</sup> Cooperatives Law, article 8(2). On the then prevailing procedure for disposing of property in cooperative ownership, *supra* n.244, p.131-132.

<sup>803</sup> Cooperatives Law, article 7(4).

<sup>804</sup> See Cooperatives Law, articles 1(2), 8(1) and 29(1).

<sup>805</sup> *Supra* Section 2.3.

<sup>806</sup> Cooperatives Law, article 8(1).

<sup>807</sup> Cooperatives Law, article 29(1).



participants in the economy.<sup>808</sup> Thirdly, it was the first time that this (or any) form of ownership was applied so visibly to an *industrial* organisation.

In this second expression of the participation model, the state lost its second element of the confirmation governance regime, its status as "property-owner". The most narrow effect of this was that the state lost its right to limit the possession, use and disposition of the property of cooperatives through "designation" as the continuing owner.<sup>809</sup> However, more broadly, the loss of ownership of the cooperatives themselves and of their property meant that the monopoly position of the state as the single legal owner of the whole industrial economy became capable of erosion as this "independent" cooperatives sector developed. It was therefore critical that the legislation on cooperatives provided some other means by which the state could still maintain control over the activities of the cooperatives in particular, and more generally over the underlying economy as a whole.

#### 6.4.4.3 *Loss of Role as Economic Sovereign (The Cooperatives Sector, Coercive Law and State Aid)*

In this second expression of the participation model, the implications of identifying an interest of the participant as "separate" from that of the state, became more radical, visible and significant: the state neither owned this industrial organisation, nor its property, and as such the state was excluded from participating in its internal management, leaving greater formal discretions in the hands of the participants. While acknowledging that the participants had a separate interest, the state did not want the cooperatives simply to become a vehicle for the pursuit of their narrow interests. The Smithean hidden hand was still mistrusted, and as in previous industrial and agricultural forms, the state needed to ensure specifically that the cooperative acted in the wider interests of the social. This was achieved partly through the registration and termination procedures. However these mechanisms only really gave the state the right to halt their activities and were not a way to control management on an on-going basis. The protection of the interests of the social and the state were therefore developed through coercive law and the limitation of rights through legislative diktat in an attempt to preserve economic sovereignty over the industrial and national economy.

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<sup>808</sup> This concept is explored in greater detail infra Chapter 7.

<sup>809</sup> See supra Section 3.4.2. Where the state did retain ownership of the property "of" the cooperative (ie where the property was exclusively in state ownership), the state did impose traditional designation restrictions. Therefore in the case of land, which was only granted for use, the state "obliged" the cooperative "to ensure the efficient use of land, manifest constant concern for increasing its fertility...and...carry out...production on the basis of low waste and wasteless technology" (Cooperatives Law, article 9(2)).



Once again an approach was taken that was rooted in collective farm law and that had been present in the first expression of this model, namely the "balancing" or "combining" interests through the use of coercive law.<sup>810</sup> The Cooperatives Law acknowledged this "balance",<sup>811</sup> and by diktat, imposed requirements on all cooperatives to take into account wider social or state interests. Article 4 set out the "principal tasks of the cooperative" in the following order "the satisfaction of the requirements of the national economy and populace...the development of labour and social activeness of members"; then, to "increase in employment of the populace in socially useful labour"; and finally, ensuring "from its own revenues an increased standard of living of members and their families".<sup>812</sup> The Cooperatives Law never really mentioned the satisfaction of the interests of the participants as a purpose of the activities of the cooperative without combining it with those of other interest groups including the state, consumers, workers, and society generally. Indeed the state's concern that the cooperative may become a vehicle for the expression of the narrow interests of the participants was evidenced by the explicit direction that "no one shall have the right to use cooperative ownership to obtain illegal revenues and for other mercenary purposes".<sup>813</sup>

While the granting of the right of ownership to an industrial juridical person (the industrial cooperative) blurred the traditional distinction between the "state owned" industrial economy, comprising state enterprises, and the "non-state owned" (but state controlled) agrarian economy, comprising collective farms and cooperatives, it did not undermine the fact that the Soviet economy continued to be bifurcated between a "state owned" and a "non-state owned

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<sup>810</sup> Supra Section 6.3.4.

<sup>811</sup> References to balancing interests in the Cooperatives Law included: article 5(1) ("the fullest combination of their interests with the interests of the collective and society"); article 10(1) ("the combining of personal, collective and state interests"); article 19(1) ("the mutual interests both of the cooperatives and consumers and the national economy as a whole"); article 17(3) ("mutual relations of the cooperative with the state, cooperative and other social enterprises, organisations, and citizens who are consumers of its product"); and article 29(2) ("the proper combining of interests of cooperatives with all-people's").

<sup>812</sup> Other references to the wider role of the cooperatives in the Cooperatives Law included: the preamble ("the use of cooperative forms in every possible way for the satisfaction of the growing requirements of the national economy and populace for foodstuffs, consumer goods, housing and various products of production-technical designation, work and services"); article 1(2) (role in "satisfying more fully the material and spiritual requirements of the Soviet people"); article 5(2) ("the cooperative has been called upon to actively participate in the economic and social development of the country...the fullest satisfaction of the growing material and spiritual requirements of people"); and article 17(3) ("the interests of consumers shall be the major requirement for the activity of a cooperative and the principal criterion for assessing the quality and efficiency of its work"). Indeed article 24(2) required the cooperative to use its own assets to construct housing, preschool institutions and other objects of social designation (it was unclear whether this was to be for the members, workforce or simply society in general).

<sup>813</sup> Cooperatives Law, article 7(4).



sector"; it was just that the state owned sector was no longer coincident with the entire industrial economy.

The state sought to extend its control over the non-state owned sector (including the 1988 cooperatives and collective farms) in the traditional way. Thus although the Cooperatives Law recognised these two sectors and sought to provide equal protection for both,<sup>814</sup> it also contemplated state control over the "cooperatives sector". This was done by continuing to conceive of the economy as a "unified national economic complex",<sup>815</sup> and then by stressing the "leading role of state (all-people's) ownership",<sup>816</sup> and contemplating an "extensive interlaced system" of cooperatives as "organically connected (*"organicheski svyazannuyu"*) to the state sector of the economy".<sup>817</sup>

As with collective farms, this "organic" connection to the state sector proved to be quite restricting. Gsovski noted that the state had always retained control in practice over these "voluntary democratic organisations" through its control over the economy as a single national complex and quoted a 1939 textbook on collective farm law: "[The status of collective farms] does not preclude governmental agencies and public organisations [i.e. the Communist Party] from recommending to the general meeting one or another comrade for the office of chairman"; and concluded "from the soviet laws and decrees, one gets the impression that all the rules designed to safeguard the autonomy and self-government of collective farms are more often violated than obeyed."<sup>818</sup>

Therefore, although article 10(2) set out the principle that "interference in economic or other activities of the cooperatives on the part of state and cooperative agencies...shall not be permitted", the Cooperatives Law in fact provided a range of rights of the state to monitor the activities of the cooperatives and control the economic system in which they operated. Furthermore, it provided, by legislative diktat, certain requirements relating to their specific operations and activities. The reality of the underlying position was acknowledged in the June 1990 Amendments which included the declaration that "the present provision shall not affect

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<sup>814</sup> The preamble to the Cooperatives Law noted "the equal interaction of state and collective farm-cooperative sectors of the socialist economy"; article 1(4) recognised both state enterprises and cooperatives as "the basic link" in the economy; and article 8(1) provided for equal protection of state and cooperative ownership.

<sup>815</sup> Cooperatives Law, article 1(4).

<sup>816</sup> Cooperatives Law, article 1(2). Indeed cooperative ownership was even described as "under the protection of the state" (article 8(1)).

<sup>817</sup> Cooperatives Law, article 3(1).

<sup>818</sup> Supra n.22 (1948), pp.755-756 (brackets added by Gsovski).



the rights of state agencies in carrying out control over the activities of cooperatives as provided for by legislation".

Initial control over the verification of cooperatives' financial and economic activities and the conducting of audits was placed with the audit commission.<sup>819</sup> Cooperatives were required to compile very detailed financial and operational reports and as a general matter submit them to state agencies in a timely manner as prescribed by legislation. More specifically, the cooperative was obliged to notify the relevant territorial state agency of all of its contemplated and actual volumes of production,<sup>820</sup> and the agencies of state administration were given the right to "verify" the work of cooperatives;<sup>821</sup> as well as the right to carry out "control" over compliance with prevailing legislation. These provisions therefore provided sufficient grounds for the state to monitor closely the activities of the cooperatives if required.

Despite the increased role of contracting,<sup>822</sup> and despite the fact that the cooperatives had the right to "autonomously plan production" and "voluntarily accept the performance of state orders",<sup>823</sup> the state nevertheless retained the right to control the entire economy (and hence the cooperatives) in two principal ways (albeit that the balance between the interests of the state and participant shifted from the first expression of this model in favour of the participant).

First, "long-term economic normative standards" of the state as developed in the context of the state plan remained binding on the cooperatives. Long-term economic normative standards were enacted in relation to: prices, taxes, interest rates on loans, payment for natural resources, and social security deductions.<sup>824</sup> Secondly, cooperatives were required "to participate in economic competition" (on terms with increased quality and reduced costs of production) with state and other enterprises with the aim of obtaining state orders.<sup>825</sup> This requirement implicitly obliged the cooperatives sector to become involved in the state sector and on terms that were most advantageous to the state. Control over the economy was additionally effected by way of the tax system (which was to be orientated explicitly toward

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<sup>819</sup> Cooperatives Law, article 14(4) and 32(4).

<sup>820</sup> Cooperatives Law, article 18(4). This was expressed as necessary in order to ensure that the cooperatives' plans were coordinated with the plans of the region as a whole.

<sup>821</sup> Cooperatives Law, articles 32(5) and 30(4).

<sup>822</sup> *Infra* Section 6.5.

<sup>823</sup> Cooperatives Law, articles 18(1) and 18(2).

<sup>824</sup> Cooperatives Law articles 18(3) and 20(2).

<sup>825</sup> Cooperatives Law, article 18(2).



incentivising the cooperatives to act in the interests of the state and the national economy as a whole).<sup>826</sup>

Of these various mechanisms, the control over prices was perhaps the most sensitive and most disabling, for true economic autonomy could never have been achieved if prices remained centrally fixed. In fact the Cooperatives Law included a specific article on prices which, rather than suggesting that they were to be set by the cooperative in order to maximise its profit, provided that they "must (*"dolzhny"*) be structured by taking into account the mutual interests both of the cooperatives and the consumers and the national economy as a whole".<sup>827</sup> This was achieved by the Soviet of People's Deputies specifying maximum levels of prices for basic consumer goods or services.<sup>828</sup> Furthermore, the prices of any contracts for a state order, or for any production using raw materials supplied pursuant to a state order, were required to be "determined in a centralised way".<sup>829</sup> Finally, penalties were provided in the event of a breach of these provisions by a cooperative.<sup>830</sup> In this manner the state's remaining monopoly over the majority of the industrial economy was leveraged upon thereby enabling it to control prices and activities in the cooperative sector.

In addition to maintaining the right to plan the economy generally, the Cooperatives Law again adopted coercive legislation, including mandatory legislative "obligations" (by use of the words "oblige", "must" and the present tense), with a view to controlling and limiting the day-to-day activities of the cooperatives and maintaining quality and efficiency.<sup>831</sup>

Conceived in this way, the cooperatives network (like the collective farm network it superseded) was intended to be an integral part of the national economy, broadly within state

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<sup>826</sup> Cooperatives Law, article 21.

<sup>827</sup> Cooperatives Law, article 19(1).

<sup>828</sup> By an amending decree in 1989, this addition was made to article 19(2) (*O Vnesenii Izmenenii i Dopolnenii v Zakon SSSR "O Kooperatsii v SSSR, Vedomosti SND SSSR* (1989), no.19, item 350 (the "**October 1989 Amendments**")).

<sup>829</sup> Cooperatives Law, article 19(3), 21(2) and 34(3). Almost all raw materials were supplied by the state and so their pricing generally came within the centrally determined regime.

<sup>830</sup> Cooperatives Law, article 19(4) (as amended by the October 1989 Amendments and the June 1990 Amendments) provided that revenue "unjustifiably received" shall be confiscated to the budget and cooperatives may be fined an amount equal to the "illegally received additional revenue". Furthermore, a consumer had the right to dissolve any contract which breached the rules relating to price fixing.

<sup>831</sup> For example, Cooperatives Law, article 4(1) ("production shall be developed...its efficiency enhanced, the improvement of product quality...and the growth of labour productivity shall be ensured, local raw materials and materials shall be involved maximally in economic turnover, and wasteless and resource-saving technologies shall be worked out and introduced"); article 23 ("a cooperative shall be obliged to strengthen accounting discipline"); and article 26(4) ("concern for the reputation of its mark must be the subject of professional pride of every member").



control and operating by taking into account the interests of the state. As such, the Cooperatives Law required that the state supported the cooperative movement "in every possible way, promote its expansion, and guarantee compliance with the rights and *legal* interests of cooperatives and their members".<sup>832</sup> Echoing the drafting of the 1922 RSFSR Civil Code,<sup>833</sup> the reference to "legal interests" again betrayed the fact that limits that were intended to be imposed (through the law of *vires* and otherwise) on the freedom of participants to pursue their narrow interests. Indeed state guidance of cooperatives' activities was expressed to be carried out "in all-people's interests".<sup>834</sup>

The state was obliged to assist in the development of cooperatives generally;<sup>835</sup> as well as more specifically, for example, to assist in the completion of necessary documentation regarding the organisation of production and labour; capital construction and other activities; financial aid, and access to research institutions.<sup>836</sup> In addition to direct aid, the Cooperatives Law included certain "paternalist" provisions evidencing the state's "concern" that members of the cooperatives may not have possessed the sufficient experience to manage them competently.<sup>837</sup>

While the role of the state as economic sovereign was therefore preserved by leveraging upon its monopoly position in the broader industrial economy and by legislative diktat, the Cooperatives Law continued to contemplate the possibility of a state agency as a defendant, a position first more fully developed in the State Enterprise Law. Cooperatives were given the right to apply to a court or arbitrazh with an application to deem any act of a state agency void

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<sup>832</sup> Cooperatives Law, article 10(3) [emphasis added]. Reference was also made to "legal interests" in articles 29(1) and 33(7).

<sup>833</sup> 1922 RSFSR Civil Code, article 57 (which referred to "legally existing cooperatives" (*supra* p.172-173)).

<sup>834</sup> Cooperatives Law, article 29(2).

<sup>835</sup> See Cooperatives Law, articles 29, 30 and 31.

<sup>836</sup> Cooperatives Law, articles 18(5); 22(2); 26(2).

<sup>837</sup> An example of general assistance is in the provisions giving the cooperatives the right to develop plans autonomously. Paternalistic drafting in the law itself explains (and requires) that such plans should be developed on the basis of the "demand" for products and the "possibilities of receiving revenue", "the effective use of...resources", "the use of progressive technologies", the consideration of "economic expenditure of raw materials", "production and distribution costs", and "labour productivity" (Cooperatives Law, article 18(1)). Another example is article 27(3), the purpose of which can only again be paternalistic: "in order to produce a product (work, service)", the law explained "a cooperative shall organise when necessary the extraction and processing of local raw materials and materials and, in the established procedure, minerals, the collection and processing of secondary resources and wastes, subsidiary agricultural production, the manufacture and repair of equipment, tools and rigging as well as firm servicing of its product". There were many other examples of such drafting. A more specific example was the introduction of the requirement to create an "insurance (reserve) fund" which not less than 5% of net annual revenue (see June 1990 Amendments). This concept was incorporated from the contract-based concession model (see *supra* Section 5.3.2).



in full or part where such act exceeded delegated competences or did not conform to legislation. In addition, the courts and arbitrazh were given the right to award compensatory losses.<sup>838</sup> This general principle was developed by providing the right of judicial review of a refusal by a state agency to register a charter and the decision to terminate its activities.<sup>839</sup> Although article 10(2) still referred to Vyshinsky's principle of "socialist legality", as the participation model deepened, so a new concept of legality seemed to emerge where the state's competences were specified and ringfenced, and where legal rights became enforceable not just against juridical persons but also against the state and its agencies.

#### 6.4.5 *The Significance of the Second Expression of the Participation Model*

The first expression of the participation model had introduced the notion of "the separate interest" into the industrial organisation. It furthermore developed the three basic pillars of the participation model: incentivisation, democracy and coercive law. In addition, its rationale reflected the policy goal of "improving" the planned economy, and it broadly left the confirmation governance regime untouched. As already noted, there was an inherent tension between recognising the presence of different interests (in addition to that of the state's) while at the same time trying to preserve state control over the entire economy by administrative means, through central planning and control over prices. This tension and balance was acknowledged in the State Enterprise Law, although it was firmly weighted in the interests of the state.

This second expression contained certain structural differences that enabled the logic of the participation model to be extended. As the cooperatives had been developed from the law on collective farms, the state neither owned them nor their property. This enabled the development of the interests of the participant in the internal management organs to be unfettered by the direct involvement of the state in the decision-making process. In addition, this loss of ownership undermined the three distinctly Soviet elements of the confirmation governance regime: the state could no longer control the cooperatives by virtue of the fact that it was their creator, the owner of their property or an economic sovereign.

The introduction of non-state owned cooperatives into the industrial economy led to a blurring of the traditional distinction between the state owned industrial economy operated entirely

<sup>838</sup> Cooperatives Law, article 10(2).

<sup>839</sup> As mentioned in Section 4.4.4.1 above, if a registering agency did not register a charter within 30 days of the application or refused registration on the grounds provided, or if a registering agency decided to terminate the activities of the cooperative, the members of the cooperative had the right to appeal the decision to a court (Cooperatives Law, articles 11(4) and 15(2) as amended by June 1990 Amendments).



through state enterprises and civil law, and the non-state owned agricultural economy operated predominantly through collective farms on the basis of collective farm law. The result was that the non-state cooperatives sector grew within the industrial economy and economic sovereignty was only maintained by leveraging upon the state monopoly of the means of production in the non cooperative sector as well as by exploiting the state's position as legal sovereign. As such, legislation provided requirements to comply with state long term economic normative standards and to take into account wider social interests. In addition, legal procedural requirements were developed to retain control over the creation and termination of cooperatives.

This second expression was the first time since the 1930s that primary legislation had contemplated the possibility of an *industrial* juridical person with the right of ownership. By excluding the state from the internal governance regime and confining the state therefore to protecting its interests through "external control mechanisms", the role of law and statute became increasingly important.

The main structural significance of this second expression was at the same time its main shortcoming. The legacy of the Soviet law on ownership and how it was applied in the context of collective farm law meant that industrial organisations acquired the right of ownership and that the state lost its role as owner of all industrial organisations. Unfortunately this same law on ownership provided no legal regime for analysing who in fact did own them. The concept of "an ownership interest" in a juridical person was absent within mainstream Soviet ownership law and as such there was no coherence to the provisions of the Cooperatives Law on stocks; responsibility; and membership fees and other contributions. Ultimately there was no real attempt to explain fundamentally the basic legal structure of this "new" juridical person.

In Soviet times this question was successfully finessed as all state enterprises were wholly owned by the state (and thus could be treated as indivisible objects of the right of ownership) and there was no need or desire to develop an understanding of ownership interests in collective farms (as this was a politically charged issue and was successfully avoided through the regime of membership). In relation to the 1987 state enterprises and 1988 cooperatives, their characterisation of associations of people (and not capital) with an emphasis on "personal participation" also meant that the question of ownership interests could continue to be finessed without any resulting significant practical difficulties. However the Soviet approach to ownership interests of juridical persons became problematic as these new industrial organisations came increasingly to act in the context of a "socialist" market with multiple



owners and investment capital. More immediately, the lack of clarity and coherence in the legal regime of ownership interests became particularly evident as legislators sought in 1989 to examine directly this area by reintroducing the concept of contract into the basic framework of the industrial organisation.

### **6.5 1989 Leased Enterprises - From Administrative Subordination to Contractual Parity**

The first expression of the participation model was based on the formal acknowledgement of the "interest of the participant" as separate from that of the state. In the second expression, this "interest" broke free and captured the ownership of the industrial organisation itself thereby dismantling the confirmation governance regime. Increasingly the state came to rely upon its legislative sovereignty, exercised by way of coercive law, in order to maintain its economic sovereignty, and hence "administrative control", over the economy. This third expression was the most advanced form of the participation model as the state retreated from the economic incidents of its ownership of the state enterprise, retaining only a reversionary interest. In addition, the legislation on lease contemplated the creation of a new post-command economy based on contract and a permissive regime.

The leased enterprise was the most radical attempt yet to incentivise the workers of a state enterprise by giving them the ability to lease an enterprise as a whole. The rights of the labour collective to residual profits and to manage the operations of the leased enterprise were significantly greater than those in the first expression; and more importantly those rights were created by virtue of legal *contractual* relationships with the state, rather than on the basis of administrative ones.

Analysing industrial organisations and group structures on the basis of contract is something that is relatively established within market economies.. Where ownership interests are in turn owned by juridical persons, this gives rise to group structures (ie the holding company - subsidiary relationship). Within this framework, the lease "of an enterprise" would be achieved by the lease or lending of all of the ownership interests of that enterprise to another. There is no reason at all for this to affect the juridical status of the underlying enterprise, because a lease *per se* only involves ownership interests passing to another for a fixed period, and not a change in the nature of the juridical person itself or the nature of the ownership interests themselves.

By contrast, since at least the 1930s, Soviet law had rejected a "law of property" and instead constructed a "law on ownership" founded upon the forms of ownership and the identity



principle.<sup>840</sup> The forms of ownership regime took an entirely different approach and rejected the generic owner by distinguishing between the *identity* of different owners, and allocating to each identified owner a different form of ownership, together with a specific type of juridical person. Thus, for example, the law on ownership distinguished the state, created the form of "state ownership", and allocated the "state enterprise" to that form (and hence only the state could own a state enterprise).

Because the leasing of a state enterprise involved the passing of the economic incidents of ownership to multiple persons that previously had not been identified by the forms of ownership regime as owners of that specific juridical person, the legal mechanism of the lease by definition implicitly challenged the very basis of the existing Soviet ownership regime. Rather than taking-up the challenge and questioning the relevance and use of the existing forms of ownership doctrinal framework within the context of leased enterprises and the new post-command economy, the FPLease continued to regulate the leasing of state enterprises from within the logic of the traditional forms of ownership regime. In trying to make sense of the legislation and the existence of the leased enterprise, it seems as if the underlying rationale had been developed as follows:

When a state enterprise was leased to another for a period of time, the identity of the owner (or strictly speaking, the persons having the economic incidents of ownership) of the enterprise changed. The "forms of ownership regime" was predicated upon the identity principle that provided that a change in the identity of the owner changed the nature of the juridical person itself. Therefore in order to preserve the link between each specific category of owner and a single specific juridical person, the logic of the forms of ownership regime dictated that upon the signing of the lease contract, the state enterprise should change its character because the identity of the "owner" had changed. Hence, the legislation provided for the creation of a new juridical person in its own right, the leased enterprise.<sup>841</sup>

This understanding illustrates the sharp contrast between an analysis of the lease mechanism under the forms of ownership regime and under market economy principles based on the generic owner where no change to the nature of the juridical person is occasioned by the leasing of all of its ownership interests to another.<sup>842</sup> The fact that the leased enterprise existed

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<sup>840</sup> Supra Section 2.3. This is examined in much greater detail in Chapter 7.

<sup>841</sup> The detail of this process is considered infra Section 6.5.2.2.

<sup>842</sup> In fact, with the adoption of the 1995 Russian Civil Code (Part 2), the leased enterprise was reconceptualised along more traditional lines: ie as a contract where the object was simply an existing enterprise or part thereof (article 656 *et seq*) "without the committing to it any type of autonomous organisational form of juridical person" (*Grazhdanskii Kodeks Rossiiskoi Federatsii, Chast' Vtoraya*,



at all as a juridical person in its own right was therefore a result of extending the traditional Soviet forms of ownership regime based on the identity principle to apply to a situation that had never before been contemplated within that framework; for in the context of the command economy there had been no need to develop understandings of juridical persons with multiple owners that cut across the forms of ownership and no need to develop a law on group structures based on ownership relationships/ownership interest.

#### 6.5.1 *Group Structures in the Soviet Command Economy - a Summary*

It is necessary to summarise the Soviet law approach to group structures in order to understand how the contractual relationship of the lease was straightjacketed by the doctrinal imperatives of the forms of ownership regime resulting in the creation of a new type of juridical person, the leased enterprise.

Group structures in the traditional Soviet industrial economy were based primarily on administrative relationships. Indeed Soviet primary legislation did not even use the word "subsidiary" ("*dochernee predpriyatie*"). The absence of group structures based on an ownership relationship (ie "holding company-subsidiary") was primarily due to the fact that state enterprises simply did not have the right of ownership. Therefore, as a matter of law, they could not "own" another enterprise (or the ownership interests in another enterprise, had they existed).<sup>843</sup> All enterprises were treated as an *indivisible objects* of the law on ownership, and all enterprises were owned by the state. In addition, and perhaps as a consequence, Soviet law did not contain the concept of the "ownership interests" of a state enterprise, and as such did not have a developed mechanism of analysing group structures in terms of an ownership relationship.

Nevertheless Soviet law did contemplate group structures between juridical persons. However, they were developed by exploiting the possibilities of the state-owned planned economy. In a planned economy where all enterprises and agencies are in the control and ownership of the state, "*administrative instructions*" of the state, or of a state-owned enterprise duly empowered by the state, could have been given to another state-owned person, irrespective of whether the instructing enterprise had the right to vote within the management organs of the other by virtue of an ownership (eg shareholder) relationship.

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*Tekst, Kommentarii, Alfabetno-Predmetnyy Ukazatel'* (Mezhdunarodnyi Tsentr Finansovo-Ekonomicheskogo Razvitiya), p.341). As one commentary noted: "in our time the list of organisational-legal forms of commercial organisations does not include within it the leased enterprises..." (*Kommentarii Chasti Vtoroi Grazhdanskogo Kodeksa Rossiiskoi Federatsii* (Firma Gardarika:1996), p.95.)

<sup>843</sup> Which in turn was due to the fact that the Soviet state was to be the monopoly owner of all of the means of production (supra Sections 2.3.1 and 3.4.2).



The Soviet group structure relationship based on administrative links was described by the legislation as a juridical person (as an indivisible whole) being "subordinated" ("*podchineno*") to, or "within" ("*vkhodit*"), another. In the same way that a ministry had control over (but not ownership of) enterprises subordinated to it through the right to issue administrative instructions within its competence, Soviet law extended this type of relationship to apply as between industrial organisations.<sup>844</sup> Where a group of enterprises were subordinated to another industrial organisation, this latter organisation was generally called an "association".<sup>845</sup> However traditionally Soviet law used a number of names for this umbrella group concept.<sup>846</sup>

Soviet civil law did contemplate a non-administrative relationships between an industrial organisation and its structural subdivisions ("*podrazdeleniya*") or "internal links" ("*vnutrennye zvena*") that *did not* have juridical personality. The two principal subdivisions were the branch ("*filial*") and the representation ("*predstavitel'stvo*") and their status was governed by the civil codes of the 1960s and subordinate legislation.<sup>847</sup>

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<sup>844</sup> On the governance regime, see Section 3.4. More specifically see, *Effectivnost' Zakonodatel'stva O Proizvodstvennom Ob'edinenii v Promyshlennosti* (Izdatel'stvo Nauka:1981), pp.132-138.

<sup>845</sup> The effect of the association was simply to interpose an additional administrative relationship between a state superior agency and an enterprise thereby creating the triple link structure of ministry-association-enterprise. Under the Production Association Statute, although article 1 provided that "production entities comprising the production association...shall not be juridical persons", article 6 permitted that "when necessary, by decision of the respective ministry...individual independent enterprises and organisations enjoying the rights provided for by the Statute on Socialist State Production Enterprise [ie including the right of juridical personality] may be subordinated to a production association". The subordination concept was also elaborated in article 10 of the Enterprise Statute.

As has been described in Chapter 3, the origin of the "associations" dated to the syndicate movement of the late 1920s and formally to the decree of 5 December 1929 "On the Reorganisation of the Management of Industry" (O Reorganizatsii Upravleniya Promyshlennost'yu, supra n.51, p.136. The syndicate movement enabled the production of all enterprises in the same sector of the economy to be coordinated and sold through a single institution thereby enabling the extraction of monopoly profits within the NEP economy. This single institution, or syndicate, developed into the association. The relationship between the syndicate and the enterprises was initially based on civil contract law, however as the syndicates grew in size and importance and as the Soviet economy developed along the lines of the first five year plan, the relationship became confused. Thus the "association" of the 1980s was still legally separate from the enterprises within its structure, but given the right by the state to control certain co-ordinated activities through the operation of the dynamics of the planned economy and the issue of "administrative instructions".

<sup>846</sup> These include the trust, combine, firm, consortium, concern and union. No broadly accepted definitions of these concepts appeared in the legislation, however secondary material sometimes attempted to draw distinctions.

A commentary to the Enterprise Statute (compiled before the adoption of the Production Association Statute) distinguished between trusts, combines and firms on the basis that the trust comprised subdivisions in the same branch vertically integrating production; the combine comprised subdivisions from various branches of the economy, and the firm has no special management apparatus, only a factory head (supra n.245, p.28).

<sup>847</sup> There were no specific references to the branch and the representation in the 1922 RSFSR Civil Code; and therefore it is no surprise that the 1929 "Encyclopedia of State and Law" compiled under the general editorship of Stuchka also did not contain any such references (*Entsiklopeidiya Gosudarstva i Prava* -



Following the adoption of Decree 49, the cracks began to appear in this traditional Soviet understanding of the group structure. Decree 49 required a sharper focus on the ownership relationship (if any) because this was the first time that the law was forced to regulate the creation of a juridical person outside the planned economy by juridical persons that were not all state-owned. As such, the relationship between the participants (juridical persons) and the joint enterprise could not have been based purely upon administrative mechanisms. While it was uncertain who (if anyone) owned the joint enterprise,<sup>848</sup> article 18 of Decree 49 did take the first tentative steps towards recognising the concept of groups based on ownership relationships rather than administrative links by referring explicitly (in addition to the traditional branches and representations which were not juridical persons) to "branches...which are juridical persons". At the time, that formulation (and the choice of the term "*filial*" in that context) was at direct variance with the traditional doctrinal understanding of the branch as a subdivision without juridical personality. It did hint at the development of group structures based on a mechanism other than "subordination", and the

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(Izdatel'stvo Kommunisticheskoi Akademii: (3 volumes) 1929-1930)). Their formal status was only acknowledged by subordinate legislation of 1935 (O Poryadke Otkrytiya i Registratsii Filialov i Predstavitel'stv Kozyaistvennykh Organizatsii i Predpriyatii, 12 *SDZ SSSR* 90) which equated branches with departments, offices, and agencies. Initially the separation between the branch and the representation was unclear. For example, the definition of "Branches of Juridical Persons" in a 1953 Legal Dictionary (compiled before the adoption of the 1960s civil codes) included all subdivisions (offices, departments, agencies and representations) within the definition of branch merely distinguishing between them on the basis of whether they operate on internal *kozraschet* (supra n.65, p.740).

However following the 1960s civil codes, the distinction and difference between the branch and the representation became relatively settled and the procedures of the 1935 Decree were finally updated by a statute of 1982 (Polozhenie o Poryadke Sozdaniya, Reorganizatsii i Likvidatsii Predpriyatii, Ob''edinenii, Organizatsii i Uchrezhdenii, *SP SSSR* (1982), no.25, item 130). As such, the branch carried out transactions and other business in the name of that juridical person, but usually in another location; and a representation did not carry out business but merely "represented" and furthered the interests of the juridical person.

Although the branch and representation were terms of art specifically mentioned in the civil codes (see, for example, RSFSR CC, article 31), as in the case of group structures between juridical persons, Soviet law used a plethora of terminology to describe the subdivisions within a juridical person in addition to the "representation" and the "branch". Examples included "*otdelenie*" (department); "*agenstvo*" (agency); "*punkt*" (post); "*kontor*" (office); "*baz*" (depot); "*byuro*" (bureau). Article 93 of the Enterprise Statute included references to "shops, sections, sectors, production units, economic units, farms and other structural subdivisions of the enterprise" which operated in accordance with statutes, confirmed by the director of the enterprise.

Unlike the representation and the branch, these other terms did not have a precise meaning and were explained differently by different secondary materials. For example a 1965 commentary to the Kaz CC classified departments and agencies (as well as offices, depots) as essentially the same as branches (supra n.284, p.63); whereas a 1988 commentary to the same article of the Kaz CC equated departments and agencies with representations (supra n.250, p.69).



development of a new term of art for the "subordinated entity" that was later to become the "subsidiary".

In the context of the development of group structures based on ownership interests, in the period to 1989 Soviet law came to recognise expressly the existence of the "stock". The stock can be dated to the Petrine period and was treated as an equity ownership interest of a juridical person (eg of a joint-stock society), capable of being traded and listed. During the *perestroika* period, the term "stock" appeared in the Cooperatives Law, however its use was more consistent with a debt security than that of an equity ownership interest.<sup>849</sup> This may have been partly due to the fact that the socialist forms of ownership regime precluded a coherent understanding of the ownership interest of a juridical person and thus, while there was a clear desire to enable juridical persons to raise finance through the issue of securities, there was not a sufficiently developed legal framework for analysing the nature of those securities in terms of equity.

The right to issue stock was formalised by a decree of the government of October 1988.<sup>850</sup> This decree noted the right of cooperatives to issue stocks, and gave the right to issue stocks to state enterprises operating, in accordance with the State Enterprise Law, on the basis of full *khozraschet* and self-financing. The preamble set out the expressed aim of issuing stock: to "further deepen the democratic principles of management and the development of the initiative of the labour collective and every worker, permitting them to show themselves as full proprietors as well as to create the necessary economic and legal conditions for the attraction by enterprises and organisations of free resources of workers, other enterprises and associations for the financing of expenses not covered by their own financial resources...". This extract of the preamble seemed to suggest that the issue of stock had an effect on management structures by enabling workers to show themselves as "full proprietors". However the use of the term "proprietor" did not necessarily entail ownership,<sup>851</sup> and the operative aspects of the decree focussed only on the procedures relating to the issue of stock, rather than the nature of the stock as an equity or other interest. The penultimate paragraph of the decree then provided that the issue of stocks shall constitute "a form of mobilising cash resources and shall not change the status of the enterprise (organisation)". So, the legal analysis of the "stock" continued to be ambiguous, and by 1989, group structures based on

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<sup>849</sup> Supra Section 6.4.1.

<sup>850</sup> O Vypuske Predpriyatiyami i Organizatsiyami Tsennykh Bumag, *Postanovleniya* (October 1988), no.1195, p.83.

<sup>851</sup> It did in the case of the cooperatives (supra n.803) but did not in the case of 1987 state enterprises (supra n.656 and 715).



administrative links still persisted, with no clear alternative mechanism for regulating groups on the basis of an ownership relationship.

#### 6.5.2 *Group Structures based on Contract - the Leased Enterprise*

The lease was defined as "the fixed-term possession and use for remuneration of...property...based on contract"; and the principal elements of any lease arrangement, including the leased enterprise, involved a lessor, a lessee and the leased object.

The provisions in the FPLease relating to the parties to lease contract, the creation of the leased enterprise, and its legal nature, were extremely brief and in places simply inadequate for any sensible understanding to be developed.

The brevity in part was due to the fact that the FPLease were only "fundamental principles". "Fundamental principles" was the highest form of all-union Soviet legislation below the constitution and were intended to set out broad all-union principles in a particular area of law which were then to be elaborated in more detail in the various republic codes.<sup>852</sup> For this reason, and in contrast to the legislation that formed the basis for the other expressions of the participation model, the FPLease only set out very "high level" provisions or principles. No republic codes on lease were in fact ever subsequently adopted (either during Soviet times or thereafter), and as such any analysis of this final expression of the participation model must be based primarily on the 1989 FPLease itself.<sup>853</sup>

The mere status of the FPLease as "fundamental principles" did not however account for the ambiguity or uncertainty of some of the drafting. This seeming lack of a coherent doctrinal framework in part would have been due to the fact that the orthodox lease structure sat uncomfortably within the Soviet forms of ownership regime, and lent itself to an analysis in terms of ownership interests being transferred for a period of time without affecting the underlying nature of the juridical person in question.

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<sup>852</sup> Supra Section 2.1.

<sup>853</sup> Arguably the rules relating to the property hire ("*imuchshestvennyi naem*") in the 1961 FPCivL (articles 53-55) and civil codes (eg RSFSR CC, articles 275-294) applied to the leased enterprise due to the past practice of using these words "property hire" and "lease" interchangeably (supra Section 6.1.4). It seems however that on this occasion the "leased enterprise" and "property hire" were different legal constructs. First, in the absence of a contrary indication, it is assumed that different words (leased enterprise and property hire) gave rise to different forms and legal regimes; particularly because no mention was made in the FPLease of property hire as a similar relationship; and being "fundamental principles", they therefore contemplated the subsequent adoption of civil codes specifically on lease (leaving property hire to be regulated by the civil codes). Secondly, the provisions of the legislation on property hire were at times at variance with those of the FPLease. For example a property hire contract could not exceed 10



#### 6.5.2.1 *Parties to the Lease Contract - the State as Lessor and a new Juridical Person as Lessee*

In the context of the lease of a state enterprise, it was the state that acted as lessor through a duly empowered agency.<sup>854</sup> The lessee of the state enterprise was specified in the FPLease to be a new juridical person called the "organisation of lessees". There is of course no particular reason why a new juridical person needs to be created under a legal system for the specific purpose of leasing an enterprise - unless the lease structure is to be developed from within the existing logic of the Soviet forms of ownership regime.

The leased enterprise was conceived as a more radical form of the first expression of the participation model, developed in an attempt to incentivise further the labour collective. As such, the same participant, the labour collective, was intended to be the lessee. Unfortunately the labour collective was not a subject of civil law;<sup>855</sup> and although each member of the labour collective (ie each worker) could have signed the lease contract as a "lessee", this approach would have compromised the characterisation of the state enterprise as a *single* object with a *single* owner (or holder of the economic incidents of ownership). Moreover, as a practical matter, it would have been very difficult to have had thousands of workers signing the lease contract; and as a doctrinal matter, the forms of ownership regime based on the identity principle had no precedent or straightforward mechanism for analysing the ownership of a juridical person by multiple owners.

In order to avoid these issues and preserve the one owner-one object analysis for state enterprises, the FPLease had to create a "new" juridical person, formed by the labour collective/workers, that could act as the lessee in the contract for the lease of a state enterprise. This "new" juridical person was the "organisation of lessees".<sup>856</sup>

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years, whereas contracts for the lease of an enterprise under the FPLease were of a long term nature and automatically renewable (infra Section 6.5.4).

<sup>854</sup> The FPLease contemplated the creation of state agencies specifically empowered to lease state enterprises (FPLease, article 16(1)). Where the relevant property was in the ownership of the USSR, the USSR-lessor acted through the State Property Fund of the USSR formed pursuant to the edict of the President: Ob Obrazovanii Fonda Gosudarstvennogo Imushchestva SSSR, *Vedomosti SND SSSR* (1990), no.33, item 633. The fund determined the value of property to be leased and the protection of the interests of the state.

<sup>855</sup> The 1983 Law on Labour Collectives (supra n.558) finessed the issue and avoided specifying explicitly the nature of their juridical status.

<sup>856</sup> In addition to the "organisation of lessees", the FPLease contemplated an "association of lessees" (FPLease, article 6). The provisions relating to the association of lessees were as brief as those relating specifically to the organisation of lessees. Lessees were given the right on a voluntary basis to form ("*obrazovvat'*") "combinations, unions, consortiums, concerns and other associations" and to freely



While the organisation of lessees was explicitly described as an "autonomous juridical person" in the FPLease, its creation and function were only regulated by one sub-section of article 16 of the FPLease, and as such many fundamental questions as to its nature and operation were simply left unanswered. In fact, only three aspects of the organisation of lessees were provided for in the FPLease: first, it was "formed" ("*obrazovat*'") by the labour collective; secondly, it was formed pursuant to a decision by a two-thirds vote of the members of the labour collective; and thirdly, such decision on its formation could also specify its management organs.

The FPLease therefore left almost every aspect of this juridical person to be regulated by its charter and subordinate legislation. Although the presence of this new juridical person (the organisation of lessees) meant that there could be a "single" lessee of the state enterprise, the multiple ownership problem was as a result simply abstracted to the level of the organisation of lessees itself. In this regard the FPLease was silent on the principal questions of who (if anyone) "owned" the organisation of lessees and by what legal mechanism? and whether the organisation of lessees had the right of ownership itself?

On the issue of the ownership "of" the organisation of lessees, it was uncertain as to whether Soviet law intended there to be a definite owner (as in the case of the state enterprise) or intended to finesse the ownership question by focussing on the concept of membership (as in the case of the collective farm and cooperative).<sup>857</sup> The only hint that the organisation of lessees may have been "owned" by each of the members of the labour collective was the reference in article 21 of the FPLease to "contributions of members of its labour collective" ("*vkladov chlenov*") in cash and in property. These "contributions" could have been viewed as a term of art for an ownership interest.<sup>858</sup> Alternatively, the organisation of lessees could have been intended to have been understood in terms of membership (rather than ownership) relations, particularly as its "participants" were even called the *members* (of a labour collective) thereby using the same terminology as the participants of a collective farm.

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withdraw ("*vykhodit*'"). It was unclear whether or not the "organisation of lessees" was just an example of an "association of lessees", although the association of lessees was not specifically expressed to be a juridical person.

<sup>857</sup> The analysis of the "ownership of" collective farms and cooperatives seemed to constitute a distinct approach where, in contrast to the analysis of the state enterprise, traditional doctrine overlooked ownership relationships of the juridical person in favour of an analysis of the concept of membership and ownership by that juridical person (supra Sections 2.4.2, 6.4.1, 6.4.4.2 and infra Section 7.4.2.2).

<sup>858</sup> On the possibility of contributions giving rise to ownership interests, see the analysis in relation to joint enterprises (supra Section 5.4.2.1) and cooperatives (supra Section 6.4.1).



Irrespective of whether the organisation of lessees was owned or based on a membership type relationship, it was also unclear as to who those owners or members ultimately were. Did they include members of the labour collective who did not vote in favour of the decision on the formation of the leased enterprise? Did they include new workers and exclude former workers? If so, what was the mechanism to enable changes to the ownership/membership structure as a result of changes to the membership of the labour collective?

While the issue of "ownership of" the organisation of lessees was entirely uncertain, it seemed relatively clear that the organisation of lessees did not have the right of ownership as it, like the state and the contract-based concession enterprises, did not fall within one of the existing forms of ownership as set out in the Brezhnev Constitution. However the provisions of the FPLease hinted at possible "new" forms of ownership, and it may have been intended that the organisation of lessees would come to fall within one of those new forms.<sup>859</sup>

The gaps in the analysis of the nature of the "organisation of lessees" was not of primary importance because its place in the lease process was only as a transitional vehicle: While there were no specific provisions relating to its termination, the FPLease provided that the organisation of lessees acquired the status ("*priobretaet status*") of the leased enterprise upon the signature of the lease contract.

#### 6.5.2.2 *The Object of the Lease Contract and the Creation of the Leased Enterprise*

While the characterisation of the state enterprise as a single indivisible object suited the purposes of a command economy based on the forms of ownership regime, it made the legal analysis of the lease of a state enterprise quite strained.

As aforementioned, in a market economy regime, the distinction between ownership interests and the juridical person meant that the leasing "of a juridical person" could be achieved by the leasing of the ownership interests to another, without affecting the property, rights and obligations<sup>860</sup> of the juridical person itself. The veil of juridical personality was intact. By contrast, the state enterprise did not have any ownership interests which could have been analysed as being "leased" - it was a single indivisible object. As such, Soviet law found it difficult to make the distinction between the two following approaches:

- (i) leasing (the ownership interests of) the state enterprise as a whole, and

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<sup>859</sup> Infra Section 6.5.3.2 and n.870.

<sup>860</sup> Adopting the Soviet law distinction between "rights" ("*chose*") and "things" or "property" ("*res*"), supra n.160 and 519 and infra n.912.



- (ii) leasing all the rights and obligations of the state enterprise as well as the property allocated to it in operative management.

The latter approach seemed particularly problematic because it involved the transfer of obligations, which as a strictly legal matter would have required the consent of each beneficiary.<sup>861</sup> However, in the Soviet context this was less of a problem in practice, particularly because the owner and lessor of the state enterprise itself (ie the state) was also the owner of all of the property allocated to it; and also because most of the obligations owed by the state enterprise would have been in favour of the state or other state-owned enterprises. Finally, the transfer of entities within the command economy had been achieved historically by way of administrative orders in the context of the group structures regime outlined above, and therefore, in this regard, less attention was paid to narrow legal impediments.

The mechanism of leasing an enterprise as analysed in terms of the first approach set out above was the cleanest and most consistent with the notion of the state enterprise as a single indivisible object. However, due to the lack of the distinction between ownership interest and the juridical person, the legislation was forced to develop the mechanics of the creation of the leased enterprise partly in terms of the second approach.

Article 3 of the FPLease included "enterprises" ("*predpriyatiya*") among the specified objects that could have been leased, as well as property of enterprises including individual buildings, installations, equipment and other material valuables. This seemed to contemplate the possibility of leasing the enterprise as a whole separately from leasing its property; and it was the lease of the former that gave rise to the so-called leased enterprise. Thus the FPLease referred to "in the event of a lease of an enterprise ("*pri arende predpriyatiya*")"; "a state enterprise which has been leased"; and "the lease of state enterprises".<sup>862</sup>

The procedure for leasing an enterprise involved the following steps: the organisation of lessees jointly with the trade union committee prepared a draft lease contract and presented it to the relevant state agency. The agency was obliged to consider the draft within 30 days and any disagreements were referred to state arbitrazh. The contract was then signed.<sup>863</sup>

The legal analysis of the consequences of the signature of the lease contract was steeped in traditional Soviet understandings rooted in the forms of ownership regime based on the

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<sup>861</sup> For example, RSFSR CC, article 215 ("The transfer by a debtor of its debt to another person shall be permitted only with the consent of the creditor").

<sup>862</sup> FPLease, articles 9(2), 16(3) and 16(6).

<sup>863</sup> FPLease, article 16(1).



identity principle. Two principal concepts applied: First, as explained at the beginning of this Section 6.5, the application of the identity principle meant that following the signature of the lease contract and a change in the identity of the owner (or the holder of the economic incidents of ownership) of the state enterprise, the nature of the juridical person was treated as having changed. Secondly, as the state enterprise was conceived as an indivisible object, the application of an analysis of the lease mechanism in terms of leasing ownership interests was precluded. The picture was inevitably going to be very confused:

The mechanism for the creation of the leased enterprise set out in article 16(1) seemingly was based on the traditional Soviet distinction between "property (*"imushchestvo"*)" (allocated by way of operative management) and "property rights (*"imushchestvennye prava"*) and obligations" of the state enterprise.<sup>864</sup> Therefore it provided that in relation to property: "after the signature of the contract, the organisation of lessees shall *accept* the *property* of the enterprise in the established procedure and shall *acquire the status of* a leased enterprise" [emphasis added]. Article 16 elaborated further in relation to the rights and obligations of the state enterprise: "a leased enterprise shall become the *legal successor* of the *property rights and obligations* of the state enterprise assumed in the lease... The lessor may assume fully or partially the repayment of credit indebtedness of the enterprise... The obligations of a state enterprise...shall be performed by the lessee... To the lease enterprise shall pass the rights and obligations of the leased state enterprise with regard to participation in socio-economic development of the territory on which it is located" [emphasis added].

Such provisions immediately displayed the tensions between the lease process and its analysis within the forms of ownership regime. It was uncertain what was being leased (was it the state enterprise as a whole, or the aggregate of its property and its property rights and obligations?); and if the lease contract resulted in the transfer of the property, property rights and obligations of the state enterprise to the lessee, did the state enterprise remain in existence (as a sort of "shell enterprise"), available to accept a re-transfer at the end of the term of the lease? In addition to the nature of the leased property, the nature of the parties seemed to be affected by the signature of the lease contract. The legislation attempted to preserve the logic of the identity principle by providing that upon the conclusion of the lease contract and a change in economic owner, the organisation of lessees was somehow "transformed" into the leased enterprise by "accepting" the property of the enterprise and becoming the legal

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<sup>864</sup>

Supra n.860.



successor of the property rights and obligations of the state enterprise.<sup>865</sup> Yet the process of this transformation was left implicit without adequate explanation.

### 6.5.3 *The Ownership Regime of the Leased Enterprise*

While the concept of "transformation" of the organisation of lessees into the leased enterprise can be understood as a function of the logic of the forms of ownership regime, the detail of the FPLease left many consequential issues unanswered. Most importantly, the provisions of the FPLease were entirely insufficient even to hint at the basics of the nature of the legal relationship between the labour collective and the leased enterprise (following the transformation of the organisation of lessees). As in the case of all the previous new industrial organisations, including the organisation of lessees itself, the forms of ownership regime was found lacking, unable to offer even a rudimentary legal analysis of group structures based on ownership relationships, and of the ownership of a juridical person by multiple owners. Furthermore, the question of whether the leased enterprise itself had the right of ownership should have been relatively clear within the provisions of the existing form of ownership regime, but the provisions of the FPLease again were obtuse in this regard.

#### 6.5.3.1 *Ownership of the Leased Enterprise*

The members of the labour collective clearly remained as "workers" at the leased enterprise and retained a contractual relationship with the leased enterprise in this capacity. However, as in the case of the organisation of lessees itself, it was unclear whether the labour collective/its members were also intended to be the owners of the leased enterprise through the holding of an equity-like interest (like that of the state-state enterprise relationship), or whether they were just to be "members" of the leased enterprise where their holding of equity interests was uncertain (like that of the members of the collective farm or cooperative).

The lack of Soviet group structures based on ownership interests/relationships (rather than administrative links) was more relevant when the "transformation" concept was applied to the lease of state enterprises by juridical persons other than an organisation of lessees. For example, the FPLease contemplated the lease of a state enterprise by a cooperative without mentioning the requirement for the cooperative to first form an organisation of lessees (presumably on the basis that, in contrast to the labour collective, the cooperative was a juridical person and had the right of ownership). In those circumstances, the analysis presented similar issues: did the cooperative itself "accept" the property of the state enterprise

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<sup>865</sup> "Transformation" was first contemplated as a form of "reorganisation" in the 1987 State Enterprise Law and then included in the 1988 Cooperatives Law, see *supra* n.622 and 710.



and become the legal successor to its rights and obligations resulting in a transformation from a cooperative into a leased enterprise? If so, what then was the legal relationship between the members of the former cooperative and the leased enterprise? Alternatively, would the lease of a state enterprise by a cooperative (an existing subject of civil law with the right of ownership) have given rise to an ownership based group structure: cooperative - leased enterprise? This would have been difficult to express within the existing Soviet understanding of group structures based on administrative links. However, in this regard, the FPLease, like the 1988 Cooperatives Law, contemplated the issue of "securities" and perhaps they were to be used as the legal mechanism for an embryonic ownership-based group structure.

By 1989 the concepts of "securities" and "stock" had been applied in the context of cooperatives and state enterprises and might have been used to explain the legal relationship between the members of the labour collective (or cooperative) and the leased enterprise. Articles 19 and 21 of the initial redaction of the FPLease contemplated the issue of securities, but did not specifically mention the issue of stocks.<sup>866</sup> Adopting a similar rationale to that of the 1988 decree,<sup>867</sup> securities were expressed to be issued for the "mobilisation of additional financial resources" and the FPLease gave members of the labour collective a preferential right to acquire them. Securities were also permitted to be issued to a member of the labour collective "for the value of the contribution" paid by that member to "the property of the leased enterprise". Dividends were paid on the securities in an amount determined by the labour collective proceeding from the results of production and tasks for the development of the enterprise. The nominal value ("*real'naya stoimost'*") of the securities was to be determined by the charter as well as the payment of dividends to a member who was no longer employed at the enterprise.

The references to "securities" in Russian included the concept of stocks (ie equity) as well as debt instruments; and the understanding of the nature of the stock in 1989 was more developed than in 1988 when the Cooperatives Law was passed. The reference to dividends, nominal value and a payment after the termination of labour relations further suggested that the reference to securities was intended to include stock as an equity interest. However, only the word "securities", and not "stocks", was used in the FPLease; and there was no mention of whether the relationship between the labour collective was one based on ownership or membership. As such, it is possible that the FPLease only intended that debt securities would

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<sup>866</sup> Article 21 was amended to include a reference to stocks of a member of the labour collective. The amendment was made in March 1991 and an analysis of the amended position falls outside the scope of this study.

<sup>867</sup> Supra n.850.



be issued with a view to attracting investment from the labour collective in order to further incentivise their participation. Unfortunately, because the FPLease were so "short form" it is not possible to evaluate any interpretation of "securities" in light of detailed provisions on management structures or in the context of a wider relationship between the labour collective and the leased enterprise. Therefore, as in the case of the Cooperatives Law and under the 1988 decree, the position remained far from clear.

#### 6.5.3.2 *Ownership by the Leased Enterprise*

The forms of ownership regime also provided difficulties for the analysis of whether the leased enterprise itself could "own" property. Strictly speaking, like the organisation of lessees, it neither fell within state ownership nor within collective farm-cooperative ownership. Furthermore, to the extent the leased enterprise "accepted" property of the state enterprise under the lease contract, this certainly remained in the ownership of the state (ie the lessor).<sup>868</sup>

The FPLease did however cryptically include references to "ownership by the leased enterprise", "products and revenues obtained by the lessee...[being] in its ownership" and to "its [the leased enterprise's] collective ownership".<sup>869</sup> Furthermore, the FPLease used the concept of "collective ownership" to describe the ownership regime of all new kinds of enterprise that the leased enterprise could be transformed into following its purchase by a lessee, including "collective enterprise, cooperative, joint stock society or other type of enterprise".<sup>870</sup>

These few careful references to "collective ownership" and the "collective enterprise" illustrated a possible fundamental shift in the forms of ownership regime and suggested that perhaps the leased enterprise *did* have the right of ownership. It was as if the limits of the forms of ownership regime had been reached: although the mechanism for leasing an enterprise was compressed within the logic of the forms of ownership regime. The presence of the leased enterprise, and the new open economy in which it operated, seemed to necessitate the creation of a "new" form of ownership (in addition to the existing forms). Yet in 1989 this new form of "collective ownership" was still an anomaly. "Collective ownership" had not at

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<sup>868</sup> FPLease, article 9(1) ("the leasing of property shall not entail the transfer of the right of ownership to such property").

<sup>869</sup> FPLease, articles 21(1), 9(1) and 18(4).

<sup>870</sup> FPLease, article 10(2). The application of "collective ownership" to the organisation of lessees was not specifically mentioned. In 1989 the collective enterprise or joint-stock society were not regulated by specific legislation of the *perestroika* era. On the purchase of the leased enterprise, see *infra* Section 6.5.4.



the time been referred to in any other primary legislation and its existence contradicted the current forms of ownership framework which had its legal basis in the USSR constitution itself.

#### 6.5.4 *Participation, Incentivisation and Democracy*

This third expression included all the traditional pillars of the participation model: "personal labour participation" of the participants was specifically contemplated,<sup>871</sup> and the leased enterprise was constructed in the pursuit of greater incentivisation and democracy. The protection of the interests of the state was based almost entirely on coercive law, the traditional technique of the participation model.

The contractual basis for each lease enabled much scope for determining incentivisation methods on a case-by-case basis. However, the FPLease included certain specific incentivisation techniques which included: the right to lease an enterprise on a long term basis; the right to renew a lease; the right to buy the leased object; the right of lease akin to a right *in rem*; a grandfather clause; and the general right to own the fruits of the leased object.

The principal "de-incentivising" element of the lease mechanism was its principal ideological imperative, namely that ownership was not transferred to the lessee. It would have been politically unacceptable in 1989 simply to have privatised all state enterprises; so the mechanism of lease was adopted to enable the economic incidents of ownership to be transferred to the participants, ie the labour collective, while the formal right of ownership remained with the state. The fact that the state enterprise was to be returned at some later date to the lessor may have encouraged short-termism on the part of the lessees, the labour collective. Clearly the state wanted to ensure that the state enterprise was run on a "rational" basis by the lessees and not in order to maximise short term gains before returning it to the state at the end of the term. This concern was initially addressed through three interlinked rights that further compromised the position of the state as formal owner of the reversionary interest in the leased property. These rights were the right to lease on a long term basis, the right to renew the lease, and the right to buy the leased object.

Although not specifically stated, the FPLease seemed to contain the implicit "right to lease". A labour collective at an enterprise was expressed to have the right to form ("*vprave obrazovat'*") an organisation of lessees in order to create a leased enterprise;<sup>872</sup> and if the organisation of lessees submitted a proposal to the relevant state agency to lease the

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<sup>871</sup> FPLease, article 21(2).

<sup>872</sup> FPLease, article 16(1).



enterprise, the agency "was obliged" ("*obyazan*") to consider the draft within thirty days and could be sued at the state arbitrazh for any "unfounded" ("*neobosnovannym*") refusal to lease the enterprise or delay in considering the proposal. The transition of state enterprises to leased enterprises was explicitly required to be encouraged and facilitated by the state.<sup>873</sup>

A lease contract for a state enterprise was "as a rule" to be "of a long term character - five years and longer".<sup>874</sup> This was the first step towards encouraging the lessee to take a "longer term" view of its operations. Once entered into, the lease contract could only have been terminated in accordance with its terms or by a decision of the state arbitrazh or court for violation of its conditions.<sup>875</sup> Once the term of the lease came to an end, the FPLease provided that not only did the lessee have the right to renew the contract, but that as a default rule, in the absence of an application by one of the parties, the lease contract was automatically renewed on the same terms for the same period.<sup>876</sup>

In addition to automatic renewal, the FPLease also included the right to buy the leased enterprise. While the conditions were the subject of negotiation, and restrictions or prohibitions were permitted to be imposed by subsequent legislation, it was provided that any lessee "may" ("*mozhet*") buy in whole or in part the leased property or any assets available at a leased enterprise.<sup>877</sup> This right to buy was less clear than the right to lease or the right to renew as the drafting used the Russian word "*mozhet*" (may) rather than "*imet pravo*" (shall have the right). This is not surprising as the right to buy challenged the heart of the command economy and the role of the state as economic sovereign. Financing the purchase of a leased enterprise was permitted to be achieved by financial assistance from the leased enterprise: subject to implementing legislation, the FPLease contemplated the use of assets of the leased enterprise itself as sources for the purchase of the enterprise.

Incentivising the lessee to act with a long term view in managing enterprises was therefore initially developed by attempting to reduce the significance of the state's reversionary interest through the right to lease, renew and buy. Long term planning going forward was then encouraged by ensuring that any benefits of personal participation could be passed on by

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<sup>873</sup> FPLease, article 16(6) provided that "the state shall facilitate in every possible way the development of lease relations and the transition to the lease of state enterprises". This is reminiscent of the drafting of the Cooperatives Law in this respect but without any reference to that assistance being limited to *legal* interests or activities (supra n.832).

<sup>874</sup> FPLease, article 12.

<sup>875</sup> FPLease, article 13(1).

<sup>876</sup> FPLease, article 13(3) and 13(4).

<sup>877</sup> FPLease, articles 10(1) and (2).



inheritance, and by ensuring the stability of the legal regime relating to leasing. These aims were achieved by conceiving rights under a lease contract akin to *in rem* rights, and by the operation of a grandfather clause.

Soviet law had traditionally treated the lease/property hire as part of the law of obligations and not as part of the law on ownership. Moreover, the Soviet law on ownership focussed on the identity of owners, and not in the abstract on the nature of rights in relation to an object or property. As such, the FPLease was not able to achieve the treatment of lease rights as "property rights *in rem*" by virtue of an underlying principle or framework (as would have been the case within the context of a law of property). Therefore the FPLease dealt with this point by *ad hoc* explicit statutory provisions (rather than reasoning from a basis of principle), and so the description in this study as lease rights "akin to *in rem* rights" is only shorthand. It provided that a reorganisation of the lessor or a change in the owner of the leased property shall not be a basis for changing the conditions of or terminating the lease contract,<sup>878</sup> and that rights of a citizen lessee under a lease contract could be inherited and the lessor was bound to accept the beneficiary for the remainder of the term (unless the lease was conditioned on the personal qualities of the lessee).<sup>879</sup>

Going forward, the legal risk associated with long term planning was reduced further by a grandfather clause in the FPLease which provided that the conditions of the contract of lease would retain their force even when, after the conclusion thereof, "rules worsening the position of the lessee have been established by legislation".<sup>880</sup> This was clearly an important protection provision in the context of the *perestroika* economy of the late 1980s where policy initiatives changed from month to month.

Once the FPLease had significantly neutralised the effect of the state's reversionary interest and attempted to provide the preconditions for long term leasing and long term economic decision making, it then developed the traditional incentive process of ensuring that participation was rewarded. In the context of this third expression, the incentivisation of personal participation was almost a consequence of the lease framework itself for it was a basic part of the lease model that the economic incidents of ownership and economic activity accrued to the lessees. Therefore, all products and revenues received as a result of the use of the leased property, and all separable improvements to the leased property were expressed to

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<sup>878</sup> FPLease, article 13(2).

<sup>879</sup> FPLease, article 14(5).

<sup>880</sup> FPLease, article 15(4). The use of a grandfather clause was not without precedent (supra n.492).



be in the ownership of the lessee.<sup>881</sup> Furthermore, at the end of the lease term, the lessor was obliged to pay compensation to the lessee for all inseparable improvements made to the leased enterprise. In short, subject to certain restrictions,<sup>882</sup> the lessee had the right to sell, convert, exchange, sublease and generally manage the leased property and any residual profit was "at the full disposition" of the leased enterprise which had the right to determine "autonomously" the application of such profit.<sup>883</sup>

These provisions taken together attempted to ensure that the labour collective was sufficiently incentivised both to enter into leases of enterprises, and then to manage them in a "rational" manner. The detail of the management organs was set out in the charter approved by the general meeting of the labour collective, as well as in subordinate legislation and the lease contract itself. The FPLease only contained one article in this respect which stated that "management...shall be carried out in accordance with its charter, on the basis of socialist self-management, broad democracy, *glasnost*, and the participation of every member of the labour collective in deciding all questions of its activities".<sup>884</sup> Despite the references to democracy and *glasnost*, this characterisation still used the term "*socialist* self-management" which indicated the shadow of coercive law cast over the governance regime of the leased enterprise, and the placing of the leased enterprise generally within the socialist (post-command?) economy.

#### 6.5.5 *Coercive Law and Responsibility of the Lessee*

Like the other participation enterprises,<sup>885</sup> the leased enterprise was ultimately conceived within the forms of ownership regime and hence was characterised as a "socialist goods-producer". During the period of the lease, the state was no longer the economic owner of the state enterprise, nor was it the owner of the leased enterprise itself. Like the second expression of the participation model, due to the state's changing roles, the basic elements of the confirmation governance regime were no longer applicable. The state was again left principally with its role as "legal sovereign" to ensure that the activities of the leased

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<sup>881</sup> FPLease, article 9.

<sup>882</sup> See *infra* Section 6.5.5.

<sup>883</sup> FPLease, article 19(2).

<sup>884</sup> FPLease, article 17.

<sup>885</sup> The 1987 state enterprise was still clearly a creature of the command economy with a confirmation governance regime; and the 1988 cooperative enterprise was not only expressed in article 1 of the Cooperatives Law to be a "socialist...society" but was also born of "Leninist ideas on cooperative societies", as noted in the preamble. For examples of the socialist orientation of the State Enterprise Law and the Cooperatives Law, see *supra* n.565 and 566; and n.572 and 612.



enterprise did not undermine the state's core interests; and this was achieved through coercive law (ie legislative diktat) in the FPLease itself.

The FPLease protected the interests of the state in three principal ways: firstly, it attempted to ensure that the state shared directly in any economic success of the lease project; secondly, it attempted to control the activities of the leased enterprise negatively, by placing restrictions on discretions so as to ensure that the value of the leased property was preserved; and thirdly, it attempted to control such activities positively, by imposing obligations on the management of operations.

The lease payment was required to be structured so as to ensure that the state would share in any of the economic benefits gained by changing the structure of the state enterprise to one where the management of the business was delegated to the labour collective. As such, although the amount of the lease payment was a matter for negotiation as part of concluding the lease contract, the FPLease provided that the lease payment must "include part of the profit (revenue)" generated from the use of the leased property, and as a rule was not to be less than bank interest.<sup>886</sup> It seemed as if this element of the leased payment (called lease interest) was therefore intended to fluctuate depending upon the economic fortunes of the enterprise.

In addition to ensuring that the state's interests were protected by sharing in the upside of any gains, the state needed to risk-manage the downside scenario associated with the passing of its assets into the management of others. Ultimately this could only have been achieved by placing restrictions and obligations on the management of the leased enterprise in relation to certain activities.

Unlike the first expression of the participation model, the labour collective was actually *paying* the lease payment for the right to manage the enterprise and the right to receive the fruits of their management decisions (subject to a state "skim" depending on the structure of the lease payment itself). As such, any substantive restrictions on the discretions of the management would have both undermined the incentivisation structure; as well as discouraged labour collectives to enter into the lease of enterprises in the first place.

And yet the regulation of the risks associated with a down-side scenario seemingly resulted in two principles for the operation of activities that were crude, and hence pervasive, in their scope: The FPLease gave the lessee the right to sell, exchange and generally manage the leased property (ie the state enterprise) "autonomously" but *only if* it increased the "value" of

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<sup>886</sup> FPLease, article 8.



the leased enterprise (unless otherwise provided for by the lease contract);<sup>887</sup> and it did "not entail a reduction of the production-economic potential (value) of the enterprise".<sup>888</sup>

There were no specific details as to how these principles were to be applied in practice, however the FPLease included a number of sanctions. If the leased property was returned at the end of the contract in a "worse" condition than provided for, the lessee was required to pay compensation; a violation of the lease contract could have resulted in its dissolution by a decision of the state arbitrazh or court. Finally, the FPLease imposed on the parties "responsibility established by legislation of the USSR and union republics" for failure to perform or improper performance of obligations.<sup>889</sup>

The effect of these provisions, coupled with those relating to improvements,<sup>890</sup> meant that the state participated in any economic gains through a profit skim, and the lessee retained the benefit of any separable or inseparable improvements, but that the lessee was both liable for any worsening of the condition of the enterprise than that provided for, *and* was restricted from taking actions that resulted in a decrease of its economic potential or value.

These tests were of course truly evaluative in their operation. It was therefore uncertain: what was the start date for measuring a worsening of the condition or economic potential of the enterprise? were transactions to be evaluated on an individual basis, or in the context of a number of related transactions, or in the context of an entire plan or policy? was a transaction on arms' length terms necessarily one that would not reduce the economic potential of the enterprise? was a transaction in accordance with a state order, or on state prices, one that necessarily increased the value of the enterprise? In short, these provisions gave the state an enormous discretion in intervening and restricting the exercise of discretions by management if required.

In addition to imposing negative restrictions, the FPLease imposed certain positive obligations on the management of a leased enterprise. These took the form of a series of legislative coercive diktats, including the obligation:<sup>891</sup> to ensure the effective use and regeneration of natural resources; to protect the environment; to accept state orders with regard to economic links already formed (for amounts not exceeding those accepted during the year that the lease took effect); and to purchase and sell goods at the same contractual prices as those fixed for

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<sup>887</sup> FPLease, article 18(1).

<sup>888</sup> Ibid.

<sup>889</sup> FPLease, articles 9(4), 13(1) and 7(6).

<sup>890</sup> Supra Section 6.5.4.

<sup>891</sup> FPLease, article 18(2), 18(4), 18(5) and 18(7).



state enterprises. Furthermore the state had the right to carry out "control" over the activities of the leased enterprises "in the same procedure as for cooperatives".

Evaluated in these terms, the "socialist" leased enterprise was just another participation enterprise. It separated an interest out from the all-people's state (ie the labour collective). It contemplated personal participation by that interest, incentivised that interest and gave it a certain amount of management autonomy. It also represented an end to the confirmation governance regime of the former state enterprises as the state concentrated on legal mechanisms to protect its interests. Not only was its structure compressed and distorted to fit within the existing framework of the forms of ownership regime, but also the state restricted discretions and required the leased enterprise to act within the state pricing system and accept certain state orders thereby anchoring the leased enterprise to a role in a state-run economy. The participant, while benefiting directly from any production efficiencies, gains and improvements, was required to pay a lease payment and bore an open ended liability for failure.

The significance of the leased enterprise however went beyond its role as the third expression of the participation model. By contemplating a juridical person with multiple owners and with a contract-based group structure, the 1989 leased enterprises exposed the underlying limitations of the forms of ownership regime itself. In this context, the FPLease hinted at an entirely new model of economic relations that went beyond the narrow doctrinal problems of multiple owners and ownership interests. The FPLease presented, albeit implicitly and obtusely in places, an economy based on contract instead of administrative commands; an economy based on a permissive regime; and an economy based on a generic owner.

#### 6.5.6 *Contract and the Post-Command Economy*

While the state in the capacity of legislative sovereign imposed certain restrictions on the activities of the leased enterprise by coercive law, the FPLease contemplated a role for the state in another capacity - as lessor.

The state in its role as "lessor" or "contracting party" was entirely new within the Soviet framework and moved the relationship with the state from one based on administrative subordination to one based on contractual parity. The lessee had the opportunity to negotiate the deal in the context of the leased contract; and should those terms not be acceptable, the lessee could simply walk away. The contract, as the basis for constructing the juridical person and for structuring economic relations, had its origins in earlier models considered in this study.



It was argued in Chapter 4 that the grandfather of all contract-based juridical persons was the contract for joint activity, which linked pre-revolutionary associations to the simple partnership and through to contemporary Soviet law. The first "new" industrial organisation of the *perestroika* period was also based on contract, the contract-based concession enterprise (ie joint enterprises). This was however conceived as part of foreign relations law. The first time that an industrial organisation had been developed explicitly upon the domestic civil law of contract since the early 1960s (when the 1964 RSFSR Civil Code partnerships were formally abolished) was the leased enterprise. "Contractual principles" however were already evident in the second expression of the participation model.

The principles of economic activity as set out in article 17(1) of the Cooperatives Law contemplated "socialist economic operations" existing side-by-side "the extensive use of goods-money relations". "Goods-money relations" was a reference to the arena of civil law which had been so visible in the private economy of the NEP era. On this basis, the Cooperatives Law actually referred to the existence of a "market",<sup>892</sup> and "all economic operations" were expressed to be carried out "only on contractual principles" with the choice of whether to contract, and who to contract with, being left in the decision of the contracting parties.<sup>893</sup> The principle was that "the contract shall be the sole legal and economic document regulating all the said economic-production mutual relations of the cooperative".<sup>894</sup> The importance of contracting was such that the Cooperatives Law reminded cooperatives that breaches of contract would result in property responsibility in the established procedure including the obligation to compensate for losses caused. Contracting was specifically contemplated in the areas of: the sale of goods; the hire of labour; transfers of cash and other resources; the use of property granted by state, cooperative and other social enterprises; relations between the cooperative and its collective members; obtaining bank credits; the use of state research institutions; the training of personnel; the interaction between the socialised and state sectors of agriculture; relations between a collective farm and its labour collective for use of its products; and preferential acquisition of products in consumer cooperative stores.<sup>895</sup>

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<sup>892</sup> Cooperatives Law, article 1(5) referred to a "market for goods...both between cooperatives and between cooperatives and state enterprises and organisations". Other references to the market in the Cooperatives Law included: article 1(2) ("market with high quality goods"); article 26(1) ("market competitiveness").

<sup>893</sup> Cooperatives Law, article 17(3). In Soviet law "economic contracts", the choice of contract parties and basic terms were provided by the state (supra n.344).

<sup>894</sup> Cooperatives Law, article 17(3).

<sup>895</sup> Cooperatives Law, articles 17(3) and 42(1); 4(2) and 6(1); 8(3); 9(3); 12(1) and 48(2); 23(2); 26(2); 31(4), 33(2); 33(4) and 45(4).



The leased enterprise formalised this drift towards contractual relationships by actually giving rise to a "new type" of juridical person created on the basis of contract. In that sense it radicalised the contract for joint activity by recognising the state-lessor and lessee as contractual parties and then by providing for a juridical person to arise as a result thereof. The lease contract was "the principal document...concluded on the basis of voluntariness";<sup>896</sup> and the FPLease contained broad topics that were required to be addressed in the lease contract (including a description of the property leased, the term, the value of the leased property and the amount of the lease payment) as well as a number of topics whose regulation was intended to be regulated by the lease contract (including the right to sub-lease, the right to buy and certain limits on economic activity).<sup>897</sup>

Notwithstanding the existence of certain restrictions on the activities of the lessee in the FPLease,<sup>898</sup> the FPLease still stated the broad principle that it was the lease contract that was to determine any limitations on the performance of obligations, and hence provided explicitly that "Beyond the limits of the performance of obligations under the contract of lease, the lessee is entirely free in its economic activities".<sup>899</sup> In this manner, the FPLease built upon some of the principles of earlier expressions of the participation model and implicitly hinted at the existence of an entirely new economy based on a permissive regime where everything was permitted unless prohibited.<sup>900</sup> In addition to the permissive regime for economic activity, the FPLease moved towards recognising all actors within that economy as equal with identical rights of ownership and hence identical legal status: The FPLease suggested that any person could act as a lessor and as a lessee and that the significance of the different forms of ownership based on the identity principle was something that was to be of reduced significance in the context of this new economic settlement.

The definition of "lessor" in article 4 encompassed every actor within the industrial economy, whether or not it had the right of ownership; whether or not it was the state, a natural person or a juridical person; and whether or not it was Soviet or foreign. The "lessor" was a broad church including even state enterprises and indeed introduced a new term, "full economic jurisdiction" ("*polnoe khozyaistvennoe vedenie*"), to describe a new method by which they

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<sup>896</sup> FPLease, article 7(1).

<sup>897</sup> FPLease, articles 7(2), 7(5), 10 and 11.

<sup>898</sup> Supra Section 6.5.6.

<sup>899</sup> FPLease, article 11.

<sup>900</sup> A move that was contemplated in State Enterprise Law and the Cooperatives Law (supra n.792)



were allocated state property; a term that was born from the new permissive regime.<sup>901</sup> The definition of "lessee" in article 5 likewise encompassed all actors.

Not only did the FPLease contemplate the "generic actor in the economy" encompassing all persons, it also hinted at a new era of ownership relationships that had moved beyond the narrow, identity based, Soviet forms. The FPLease set out in article 9(1) the general rule that all "products and revenues obtained by the lessee as a result of the use of the lease property shall be in its ownership". This was truly dramatic: for if any person could act as a lessee, then surely the implication was that any person in the lease context had the right of ownership? The FPLease then moved on to recognise explicitly the limitations of the existing forms of ownership by expressly referring to a new form of ownership called "collective ownership".<sup>902</sup> Finally, the FPLease envisaged the lease mechanism as operating in "all branches of the national economy and...with respect to property of all forms of ownership",<sup>903</sup> contemplating associations with multiple owners "irrespective of the forms of ownership".<sup>904</sup> Building upon earlier expressions of the participation model, it now was as if the old Soviet distinctions between industry and agriculture; state and non-state juridical persons; civil law, economic law and collective farm law, were simply no longer directly relevant.

The participation model had bent the existing spine of the Stalin economic settlement to almost breaking point. In 1989 legislators still refused to tackle any fundamental shortcomings of the forms of ownership regime, opting instead to develop the lease as best they could from within it. However, implicit within the provisions of the FPLease were the footprints of an entirely new economic order; and by March 1990 the inconsistencies between economic reality and legal regulation were so great that a revaluation of the entire basic framework of ownership relations could no longer be avoided.

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<sup>901</sup> "Operative management" was a product of the traditional authorisation regime and state property allocated to a state enterprise on this basis could only be used for the purposes specified by the state (through the concept of designation). "Full economic jurisdiction" by contrast was a product of the permissive regime and state property allocated on this basis could be used for any activity unless specifically prohibited by the terms of its allocation.

<sup>902</sup> Supra Section 6.5.5.

<sup>903</sup> FPLease, article 3.

<sup>904</sup> FPLease, article 6.



## 7. **NOVOSTROIKA OR PERESTROIKA? - THE TRIUMPH OF THE ENTERPRISE (1990 OWNERSHIP LAW AND THE 1990 LAW ON ENTERPRISES)**

*"But strangest of all are the things which happen on Nevsky Prospect. Oh have no faith in this Nevsky Prospect!...It is all deception, a dream, nothing is what it seems... "*

N. Gogol

### 7.1 **The Confirmation Enterprises and the Economic Constitution of the Stalin State**

Until 1987, the most basic principles of the Soviet industrial economic legal framework had never seriously been questioned since their elaboration during the 1930s. The spine of this system comprised state ownership and state control of the means of production supporting a network of confirmation enterprises that were the addressees of planning instructions. As the English feudal crown delegated its ownership of the means of production (ie land) to tenants-in-chief through the concept of tenure without ownership, so too did the Soviet state "allocate" the means of production to state enterprises without ownership to hold by way of "operative management". Such was the economic constitution of the Stalin state.

The foundations of that system were so fundamental that they were contained in the USSR Constitution, the 1961 FPCivL and civil codes:

The Brezhnev Constitution set out the "forms of ownership", a concept that distinguished different ownership regimes on the basis of the identity of the owner. Thus the Brezhnev Constitution contemplated a form of ownership for the state, "state (all-people's) ownership"; a form of ownership for non-state owned collective farms and cooperatives, "collective farm-cooperative ownership"; and a form of ownership for natural persons, "personal ownership". State ownership was expressed to be the "principal form" of socialist ownership,<sup>905</sup> and "enterprises organised by the state" fell within this form.<sup>906</sup>

Section II of the 1961 FPCivL set out additional principles relating to the law on ownership and articles 11-13 contained the main provisions on juridical persons. The term "juridical person" was used to define "organisations" which "possess separate property; may acquire in

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<sup>905</sup> Brezhnev Constitution, article 10.

<sup>906</sup> Ibid, article 11.



their own names property, and personal non-property, rights; and bear duties; and be plaintiffs or defendants in court...".<sup>907</sup>

While there was no formal classification of juridical persons, article 11 did contain a list of juridical persons. From this list can be implied the importance of state enterprises (listed first) as well as the theoretical link between "types" of juridical person and the forms of ownership. Thus article 11 listed separately, and therefore implicitly distinguished, "state enterprises and other state organisations" from "collective farms...and other cooperative and social organisations" presumably on the basis of the distinction between state ownership and collective farm-cooperative ownership.<sup>908</sup> This classification illustrated the rigid structure of the forms of ownership regime which provided for each relevant *identified* owner an attendant specific form of ownership *and* an attendant specific juridical person. Under this methodology, there was no juridical person that could be owned by more than one identity of owner (ie state enterprises could only be owned by the state, and collective farms could never be owned by the state).

In addition to the specific listed juridical persons in article 11, there was a catch-all category which was last on the list providing for "other organisations in the instances provided for by legislation of the USSR". This catch-all category included existing juridical persons that were not listed specifically (eg foreign trade organisations) and contemplated the possible introduction of new juridical persons in the future.

Therefore, the 1961 FPCivL distinguished the "organisation" (ie the generic term used for any juridical person) from the "state enterprise" (ie a specific type of juridical person which formed the basic or primary link<sup>909</sup> in the socialist industrial spine). It was argued in Chapter 3 that these "state enterprises" are best understood within the confirmation model. For the purposes however of evaluating the reforms of 1990 and the choices that the legislators faced that spring, a number of key elements of that model and the relationship between the state and its state enterprises need to be revisited; elements that arose primarily due to the fact that *all* enterprises in the Soviet industrial economy were owed by *one* owner, the state.

- (a) Creation: The Stalin state was an economic sovereign, the owner of all of the means of production, and as such it could decide when and whether to create any enterprise

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<sup>907</sup> 1961 FPCivL, article 11.

<sup>908</sup> At the time of the enactment of the 1961 FPCivL this classification also embodied the distinction between the industrial economy and the agrarian economy; and between civil law and collective farm law (supra Section 6.4.4.2).

<sup>909</sup> Adopting the terminology of article 1 of the Enterprise Statute and Production Association Statute.



within the industrial economy simply by diktat. There was therefore no practical need for a detailed procedural law relating to their creation.

- (b) Ownership of the enterprise and the nature of its ownership interest: Again, as the state was an economic sovereign, the single owner of all enterprises, there was no need to develop a precise legal understanding of the nature of the ownership interest of these enterprises. While Russian legal terminology contained various concepts that might have been used to have described and analysed the nature of the state's ownership interest of state enterprises (including "*pai*" (share); "*dolya*" (participatory share); "*aktsiya*" (stocks); "*dolya uchastiya*" (participatory share participation); and "*vkklad*" (contribution)), none of these appeared in the legislation relating to the confirmation enterprises. Rather than adopting any of these or other precise terms, the legislation simply stated that all state enterprises were "*located in* ("*nakhodyatsya*") the exclusive ownership of the state".<sup>910</sup>
- (c) Ownership by/property of the enterprise and the nature of its rights: In order to ensure that the state remained at all times the owner of the means of production, the law on ownership explicitly provided that confirmation enterprises did not have the right of ownership of property but merely were "allocated" property by way of operative management.

Although state enterprises did not have the legal capacity "to own property", they were juridical persons and as such had the capacity to "acquire" rights.<sup>911</sup> Consistent with this approach, Soviet law used a variety of expressions relating to rights but none provided explicitly for the "ownership" of a right.<sup>912</sup> Soviet law was forced into making this distinction between "property" ("*res*") and "rights" ("*chose*") because, on the one hand, the right of ownership of "the means of production" (ie property) as a matter of Marxist-Leninist theory "had to" be denied to juridical persons (because the state was to own all the means of production); but on the other hand, to deny juridical persons the capacity to acquire "rights" *per se* would have been inconsistent with their ability "to contract" and to bear separate property responsibility from the state. In practice, little turned on whether rights were "owned" or only "acquired" by their holder because this distinction was broadly a consequence of doctrinal imperative

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<sup>910</sup> Brezhnev Constitution, article 11 [emphasis added].

<sup>911</sup> 1961 FPCivL, article 11.

<sup>912</sup> Traditional formulations in the constitution and civil legislation referred to rights "belonging" and being "extended" to a person; or of persons "having" or "acquiring" rights.



(rather than practical necessity) resulting from the closed system of the Soviet command economy where the unitary Soviet state was to be the legal absolute owner.

- (d) Management: The presence of a single owner, the state, removed the need for an internal governance regime or procedure for the balancing of the interests of different owners. The principle of one-man management further simplified the management structure: one owner appointed one manager who was responsible for all operations and could act on behalf of the enterprise. Official ideology reinforced the representative nature of this economic dictatorship by explaining that the state, as a socialist all-people's state, represented the interests of all-people. From a theoretical perspective, the state's monopoly ownership of the enterprises with one-man management was expressed to result in management being in the interests of all workers of that enterprise and of Soviet society as a whole.<sup>913</sup>
- (e) Sovereignty, responsibility and the macro economy: In addition to the state's role as owner of the enterprises and of their property, the state, as "legal sovereign", had the right to oblige the enterprise to carry out activities by virtue of legal diktat; and the state, as "economic sovereign", had the right to oblige the enterprise, together with the other enterprises within the national economy, to comply with administrative (planning) instructions.<sup>914</sup> Despite the fact that the state exercised considerable control over the activities of the enterprises, the 1961 FPCivL provided that the state was not legally responsible for their debts and vice versa. However, while the state had no formal legal responsibility for the debts of its enterprises, its *de facto* responsibility emerged as a result of the nature of the command economy: The state as owner of all enterprises ran the macro economy on the basis of a single plan and hence state subsidies were granted as a matter of course to enterprises who were, by virtue of their balance sheets, "unprofitable" where their place within the plan as a whole was considered necessary or justified (from a political or economic perspective).<sup>915</sup>
- (f) State and Communist Party control: Due to the blurring of the roles of state and Party, the exact method by which in practice the Party and the state controlled the

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<sup>913</sup> See quotation at the beginning of Chapter 6.

<sup>914</sup> Supra Section 3.4 and 6.5.1.

<sup>915</sup> State subsidisation of industry was a legacy of the financing of the first five year plan. Although it was intended that industrialisation would be financed through increased profits, this proved unrealistic and in the absence of foreign credits and a market for capital, it was ultimately the state budget that funded the capital investment industry. A practice that proved difficult to curtail within the logic of the planned economy (supra n.104, pp.740-746).



enterprises was often ambiguous. While distinctions can be drawn between the Party as "guiding and directing force" in Soviet society, and the state *qua* founder (operating through the voting system), the state *qua* property owner (imposing limited designation on the use of property), the state *qua* legal sovereign (adopting legislation) and the state *qua* economic sovereign (adopting planning instructions and state orders), it would have been difficult to have drawn such distinctions in practice. There were so many overlapping ways that the Party and state could have ensured compliance with their instructions that there was no necessity to identify the specific mechanism that was being adopted in any individual case.

These above elements summarise what has been argued to be the hallmarks of the "industrial enterprise" - an integrated devolved cog in a single administrative and economic complex expressing the interests of the state and hence "all-people". In this manner, the enterprise could perhaps be viewed as the socialist equivalent of the English eleventh century feudal tenant, representing the most basic element of the economy, the vassal or puppet of the socialist state.

## **7.2 The Challenge to Stalin Economic Constitution - 1987-1990**

Despite the principal place of the confirmation enterprise within the traditional Stalin industrial economy, as aforementioned, article 11 of the 1961 FPCivL contemplated a number of other juridical persons (operating mainly in the agricultural sector) as well as the possibility for the elaboration of new juridical persons through the catch-all category. It was to these "other juridical persons" that the regime turned in 1987 in order to develop from within Soviet law potential alternative forms that could be used in the industrial sector. These have been described in terms of the contract-based concession and participation models. Their introduction into the economy began to question, press and bend the rigid spine of the command system.

Perhaps most importantly these models contemplated the existence of new juridical persons with more than one founder. Sometimes, as in the case of joint enterprises, the state (through, for example, a state enterprise as a participant) acted as one of the founders, and sometimes (for example as in the case of leased enterprises), it did not. As a result of the presence of these new juridical persons, the basic assumptions underpinning the confirmation model and the Stalin economic constitution gradually became compromised: the state no longer was the owner of all enterprises and was no longer the sole owner of any given enterprise. The introduction of more than one founder and the possibility of a founder not ultimately owned



by the state necessitated a re-evaluation of each of the six elements noted in Section 7.1 above:

- (i): first a procedure was required by which the state could grant juridical personality upon a specific organisation following the petition of others;
- (ii): secondly, as the state was no longer the single owner, as more than one type of industrial juridical person was now contemplated, and as each identified owner could own more than one type of industrial juridical person (sometimes even jointly with other identified owners), an understanding of the legal nature of the ownership interests of the founders seemed to be required;
- (iii): thirdly, as the state no longer owned (or entirely owned) all organisations, the ownership regime of these organisations could not fall within the state ownership-operative management analysis;
- (iv): fourthly, the presence of more than one owner meant that the law setting out the procedure for the management of the organisation would need to be more elaborate, regulating the relationship between the founders and their representatives at the management level;
- (v) and (vi): fifthly and finally, these new models presided over the erosion of the power of the Party, and over the erosion of the roles of the state as owner of all enterprises and their property, and as economic sovereign. Consequently the state lost the ability to manage the economy as a single administrative matrix and enterprises were “freed” to operate on a basis where their own balance sheets became the sole indicator of their “utility”. As the roles of the state came to be confined to its position as legal sovereign, it had to reorientate and clarify its strategy for controlling the economy and the "new" industrial organisations therein by developing “legal mechanisms”, principally through the authorisation process and statutory diktat, that would ensure its interests were protected.

The new models had fissured, split and cracked, in both theory and practice, the notion of the "all-people's" state and the unity of interests in the Soviet industrial economy as the public and private spheres of the Soviet state were most “publicly” torn apart. The principles of a new open economy and a new rudimentary law on juridical persons were already latent in the legislation on which these models were based, contemplating an atomised legal entity participating as an independent actor in a market orientated economy with multiple founders who were persons other than the state.



From the point of view of the law on industrial organisations, there still remained four principal steps to be climbed before the "general corporation" could be born from the ashes of the socialist industrial enterprise:

- (a) The Concept of "the Generic Owner" and the Nature of the Ownership Interest: most importantly, the Soviet ownership regime had to be reconstituted by rejecting the socialist notion of "forms of ownership" and by embracing the concept of "the generic owner" thereby giving all subjects of civil law the identical (not just the equal or equivalent) "right to own property". This would have the effect of moving the doctrinal emphasis away in any given case from the "identity" of the owner towards the "nature of the right" owned; and move the law on ownership towards a law on property. In this way, the nature and scope of rights of an owner would come to depend upon the nature of the property owned and the rights in relation to that property, rather than upon the identity of the owner.

In the context of the juridical person, such a regime would constitute a juridical person as a subject of civil law (and not as an object) which issued ownership interests (that were objects); and where the rights associated with each ownership interest would in part define the nature of the juridical person and would determine the rights of the owner of that ownership interest *vis a vis* the juridical person. In this way juridical persons would come to be classified by reference to their specific peculiarities rather than by reference to the identity of their owner.

An ownership regime based on forms of ownership derived from the identity principle was broadly necessary and unproblematic, in both theory and practice, in an economy where the Soviet state owned all the means of production. However, in an economy with multiple owners where each identified owner has the right to own more than one type of juridical person, a classification based on the identity of the owner and forms of ownership would almost certainly prove to be comprehensively and structurally flawed. Its continued application in such an open economy would prevent, from a legal point of view, a sensible understanding of the nature of ownership interests and hence preclude the elaboration of a logical and coherent framework for characterising and classifying the general corporation and other juridical persons.

- (b) Equity Capital: if there was a shift in the focus of the law on ownership from the identity of the owner to the nature of the ownership interest, the general corporation would only be possible where the law also contemplated an ownership interest of a juridical person that was constituted in terms of an investment (ie equity capital) and



not only in terms of an obligation to participate (which characterised the participation enterprises). The introduction of equity capital, and the consequential separation of ownership from control, would entail a more detailed governance regime providing a procedure both for regulating the interests of the participants *inter se*, and the managers *inter se*, as well as for regulating the interests of the participants on the one hand with those of the managers on the other.

- (c) Right to Incorporate: an opening up of ownership rights would need to be coupled with a reorientation of the status of the industrial organisation from that of a concession to that of an “accepted” actor in a new economy. This would be evidenced by a move from an authorisation system of creation to one where founders had the *prima facie* right to incorporate, without any state approval of purposes, provided that certain registration/notification formalities were completed.
- (d) Capacity and State Control: if the law were to develop an ownership regime based on the concept of “the generic owner” coupled with the right to incorporate, techniques such as the “forms of ownership regime” or an “authorisation” procedure would no longer be available to prevent the creation of a juridical person by its founders. There are of course “legitimate” reasons for a state to regulate the “classes” of person permitted to found a juridical person (for example, those without civil law capacity (such as minors or the insane) or particular foreign investors). The regulation of the scope of the rights of those persons would have to be achieved, not through contorting the general law on industrial organisations or the law on ownership, but through stand-alone legislation by developing the civil law concept of legal capacity or by specific legislation on (for example) foreign investment (without creating a “new type” of juridical person for this purpose).

In 1990 the law on industrial organisations was at a crossroads. The contract-based concession and participation models, coupled with the other *perestroika* reforms, had bent the existing spine of the command economy to almost breaking point: either the spine could be broken and a new framework elaborated by extending the momentum and logic of these models; alternatively, the existing regime could be bolstered and restructured by bringing the new models from the fringes of the law into the mainstream but without altering fundamentally the foundations and basic principles of the then prevailing framework of the juridical person and the law on ownership. This can ultimately be characterised as a choice between “*novostroika*” (the building afresh) and “*perestroika*” (restructuring), between the market economy general



corporation and the socialist enterprise. The constitutional amendments of March 1990, the 1990 Ownership Law and the 1990 Law on Enterprises evidenced the choice that was made.

### 7.3 March 1990 Constitutional Amendments - Towards a New Economic Constitution

On 14 March 1990 the Brezhnev Constitution was amended (the "March Constitutional Amendments") again.<sup>916</sup> Certain of the amendments relating to the law on ownership, and hence to the administration of the economy as a whole, were then elaborated in more detail in the 1990 Ownership Law and the 1990 Law on Enterprises. These constitutional amendments and the two new laws should not be understood discretely as three separate enactments. Taken together, it shall be argued that they set out the basis for a new "economic" constitution for the Soviet Union, a consolidation and restatement of the previous reforms of the *perestroika* era and a manifesto for the post-Stalin economy and for the "new" industrial juridical person. The 1990 Ownership Law more specifically set out the basic features of this underlying economic constitution and its theoretical framework, and on the basis thereof, the 1990 Law on Enterprises then set out the principles upon which all the actors in the industrial economy would operate.

The March Constitutional Amendments comprised three principal changes: the contemplation of a multi-party system with the amendment of the infamous article 6; the creation of the post of President of the USSR; and changes to the law on ownership. As a consequence of the latter, articles 10, 11, 12 and 13 of the Brezhnev Constitution, which set out the fundamentals of the Economic System and forms of ownership, were replaced in their entirety.

The designation "socialist ownership" and the old forms of ownership were removed and in their stead article 10 provided for three "new" forms of ownership: state ownership, collective ownership and ownership of Soviet citizens.<sup>917</sup> It further provided that all of these "diverse forms of ownership" were subject to "equal protection".

The March Constitutional Amendments evidenced the demise of the unitary Stalin political centralised state that had comprised republics which, although legally autonomous, were by no means truly independent. The participation model had begun the process of identifying separate interests from those of the state; and now those initial steps were taken to their logical conclusion. The previously homogenising concept of "state (all-people's) ownership" became splintered in recognition of the independent aspirations of the nations and republics

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<sup>916</sup> Ob Uchrezhdenii Posta Prezidenta SSSR i Vnesenii Izmenenii Dopolnenii Konstitutsiyu (Osnovnoi Zakon) SSSR, *Vedomosti SND SSSR* (1990), no.12, item 189.

<sup>917</sup> In fact the March Constitutional Amendments listed these forms with "ownership of Soviet citizens" first, and "state ownership" last.



within the Soviet Union. Article 13 now provided for "state ownership", not as the unitary "all-people's" ownership of a single state, but as allocated separately and divided between property in the respective jurisdictions of all-union ownership, ownership of the union republics, and ownership of the autonomous republics, autonomous regions, autonomous national areas, territories, regions and other administrative-territorial entities. At a single stroke, article 13 almost by definition gave way to the notion of the fragmented state with more than one owner, at least at the level of the polity.<sup>918</sup>

As the political unity of all-people's state ownership was shattered and relocated among the constituent administrative parts of the USSR, the economic unity of state ownership of the means of production was eroded with the recognition of the right of ownership of others, including juridical persons. "Collective ownership", in accordance with article 12, expanded the form of ownership that had previously encompassed non-state owned juridical persons (ie collective farm-cooperative ownership) to embrace more widely ownership by leased enterprises, collective enterprises, cooperatives, joint stock societies, economic organisations and other associations. This form of ownership was an entirely "new form" without precedent in Soviet law,<sup>919</sup> and brought the ownership regimes of the new juridical persons from the ambiguous (as in the case of the joint enterprises and the leased enterprise) or from the fringes (as in the case of the cooperatives) into the mainstream. Additionally, similar to the references in the FPLease,<sup>920</sup> this definition of collective ownership directly contemplated the introduction of a number of further new juridical persons, including the joint-stock society and other economic organisations, for which specific legislation had not yet been adopted.

Finally the concept of "ownership of Soviet citizens", as detailed in article 11, radicalised the concept of personal ownership by permitting the citizen to use his personal property "to satisfy material and spiritual requirements and independently carry on economic and other activities not prohibited by law". This was to open the door to the possibility of offering labour for pay and hence of turning the Stalin concept of individual labour activity into a broader right to conduct entrepreneurial activity.

In short, the March Constitutional Amendments took the step of recognising the right of ownership of the means of production by entities other than the state, including by the new

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<sup>918</sup> This was explicitly acknowledged in the 1990 Ownership Law which referred to "owners of state property" (article 19(1)).

<sup>919</sup> There were references to "collective ownership" and "collective enterprises" prior to the March Constitutional Amendments" but their significance and meaning was uncertain (see, for example, FPLease, article 10(2); supra Section 6.5.3.2).

<sup>920</sup> Supra n.870.



industrial organisations. But it still remained to be seen whether these amendments were to be the stepping stone to the *novostroika* of an entirely new framework or whether they were merely a concession, a reorientation, a *perestroika*, with the aim of supporting the tenets of the *ancien* socialist regime.

#### 7.4 1990 Ownership Law - The Principles and Doctrinal Structure of the New Economy

The new forms of ownership as set out in the March Constitutional Amendments were developed in a specific "Ownership Law" enacted on 6 March 1990. This was the first time in Soviet history that a "law (*zakon*)" had been adopted detailing the specifics of the Soviet ownership regime which previously had been regulated only by broad framework principles set out in the constitution, 1961 FPCivL and the civil codes. Much has been written about the 1990 Ownership Law mainly highlighting the changes made in the positive law. Looking back at the laws on ownership of 1990, Professor Alekseev commented that they "clearly led to a new democratic, market aspect to the whole system of property relationships."<sup>921</sup> Indeed, from the perspective of positive norms and the operation of the economy, the 1990 Ownership Law introduced a fundamentally different set of rules for the law on ownership and provided for the development of a market orientated economy based on profit. However, this Section will try to search behind the positive law rules in order to analyse the effect that the 1990 Ownership Law had at the level of doctrine and attempt to understand not just how this doctrinal structure affected the economic framework, but also how it determined the basic orientation and law of the "new industrial organisations".

It shall be argued that the 1990 Ownership Law, building on the fragmentation of the single economic state in the March Constitutional Amendments, seemingly embraced the concept of "the generic owner" and formalised three "new" key principles, all of which were latent in the previous legislation and the March Constitutional Amendments. These comprised the principles of equivalence between owners, the permissive regime and the rule of law state. The formal adoption of these principles into the Soviet ownership regime was necessary in order to create a legal framework that reflected the development of the post-plan "open economy" based on profit indicators and with multiple owners. In addition they enabled the basic law on ownership to be readjusted in order to take into account and provide for the new models and the new legislation introduced since 1987 which had gradually, and then more visibly, undermined the coherence of the previous norms.

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<sup>921</sup> S.Alekseev-M.Rogozhin, *Chastnaya Sobstvennost' - Osnova Nezavisimost, Zakon* (1993), no.2, p.89.



The three new key principles and the development of a new open economy could have signalled a move in the direction of *novostroika* by facilitating the completion of the four outstanding principal steps to the general corporation noted in Section 7.2: the concept of “the generic owner” would have formalised the fragmentation of the previous unitary Soviet state and the rejection of the forms of ownership regime; the principle of equivalence of rights of all owners and equality between actors in the marketplace could have indicated the beginnings of the development of a regime where the nature of the ownership interest rather than the identity of the owner was the keystone concept; equity capital and the right of incorporation could be seen as logically flowing from the framework of the permissive regime; and the regulation of capacity through *vires* and stand alone foreign investment legislation would seem to sit comfortably within the principle of a rule of law state. However it shall be argued that while these three principles clearly enabled the *possibility* for *novostroika* and the development of ownership relations based on the “generic owner”, a closer analysis of the underlying structure of the 1990 Ownership Law leads to the conclusion that in fact the Soviet polity had opted for the more conservative choice – *perestroika*. In particular, although the 1990 Ownership Law changed each individual form of ownership, it continued to embrace the uniquely socialist doctrinal concept of the “forms of ownership regime” itself based on the identity principle. This “underlying doctrinal socialist structure” of the 1990 Ownership Law will be shown to have had profound consequences for the development of the law on industrial organisations, and it shall be argued that as a result, the 1990 reforms evidenced the triumph of the “socialist industrial enterprise” over the market economy “general corporation”.

#### 7.4.1 *New Principles - Equivalence, the Permissive Regime and the Rule of Law State*

The March Constitutional Amendments shattered the Stalin concept of the Soviet state as the unitary and exclusive owner of all the means of production and thereby introduced the possibility for a variety of juridical persons and owners of the means of production. The 1990 Ownership Law acknowledged this proliferation of the “right to own”, and initially seemed to build its regime around the concept of “the owner”. Article 1 did not differentiate between the identity of any owner, and instead provided generally that “an owner shall, at his discretion, possess, use and dispose of property which belongs to him”. This initial declaration seemed to suggest a departure from the concept of different ownership regimes applying to different types of owner and a step towards the evolution of a single ownership regime applying equally to all owners, including the state.

Developing from this definition of “the article 1 owner”, the three key and somewhat interlinked principles mentioned above can be derived from the provisions of the 1990



Ownership Law. They comprised the principles of equivalence between owners, the permissive regime and the rule of law state.

The principle of “equal protection” of all forms of ownership provided in article 10 of the Brezhnev Constitution as amended by the March Constitutional Amendments underlined the fact that the concept of “the article 1 owner” entailed not only that non-state entities had the capacity to act as an owner, but also that all owners were *prima facie* to be treated equally. Unfortunately the corresponding provision of 1990 Ownership Law, article 4(5), omitted the word “equal” and only directed the state to “ensure the protection” of the forms of ownership. Article 31(3) of the 1990 Ownership Law did however use the word “equal” in providing that the state should ensure “equal conditions for protection of the right of ownership for citizens, organisations and other owners”. The significance of the omission of the word “equal” in article 4(5) can perhaps therefore be overstated, and in any event, it is clear that by the apparent introduction of the concept of “the owner” and the move towards protection of all forms on a similar (even if not entirely equal) footing evidenced the fact that the confirmation enterprise was no longer to have a monopoly on ownership of the means of production in the industrial sphere and that the economy going forward was to be opened to a range of other actors, including citizens and juridical persons (whether state owned or not).

Orthodox Soviet law had traditionally been based on an authorisation regime (ie everything was prohibited unless specifically permitted or authorised). This authorisation regime had been gradually compromised by much of the legislation of the *perestroika* period including enactments relating to the contract based concession and participation models.<sup>922</sup> The March Constitutional Amendments and the 1990 Ownership Law, a manifesto for the new economy, reinforced and underlined this change in approach by providing explicitly for the alternative permissive regime.<sup>923</sup> This was formally set out in article 1 of the 1990 Ownership Law which, in addition to setting out the concept of “the owner”, permitted an owner to carry out all activities that were “not contrary to” or “not prohibited by” law. The permissive regime was then developed throughout the law, as appropriate.<sup>924</sup>

The move towards creating an even playing field for owners in the market place and the removal of the monopolistic position of the state accelerated the drift towards law. As the participation model illustrated, the new Soviet state, shorn of its role as sole creator of all

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<sup>922</sup> The introduction of a permissive regime seemed to be anticipated by references in the State Enterprise Law (supra n.694), the Cooperatives Law (supra n.792); and the FPLase (supra Section 6.5.6).

<sup>923</sup> Brezhnev Constitution, article 11 as amended by the March Constitutional Amendments.

<sup>924</sup> See 1990 Ownership Law, articles 14(3), 15(2), 24(1).



enterprises, of its role as owner of all the means of production and hence of its role as economic sovereign, was forced to use its last remaining role as “legal sovereign” to protect its interests. Previously “extra-legal” mechanisms, such as control by the Communist Party and use of the state’s role as owner of all enterprises, were used to supplement gaps in the scope of its legal rights. By contrast, in this new world where law was the central mechanism for ensuring compliance with state policy, the scope and content of the legal system had to be sufficiently detailed, clear and coherent to stand alone. Such an elevation in the role of law resulted in the creation of rights not just between subjects of civil law but also as against the state itself, and this was the essence of the principle of “the rule of law state”.<sup>925</sup>

While the permissive principle was stated explicitly, there was no specific declaration of the principle of the rule of law state in the 1990 Ownership Law. Again the principle of the rule of law state was latent in previous legislation, but in terms of the 1990 Ownership Law, it can be understood almost as an inevitable consequence of the two principles of equivalence and the permissive regime: as the state was relegated to just one type of owner, sitting within a regime that applied to all owners, so it sat within the restrictions of law itself and ultimately the USSR Constitution. Further evidence of the rule of law state in the 1990 Ownership Law could be seen in the substantive protections provided to the owner of property in the case of infringements of his rights by the actions of state agencies. The 1990 Ownership Law directly contemplated the challenge of state acts that exceeded specified competences and the declaration by the courts and state arbitrazh of such acts as void together with the possibility for granting compensation for losses.<sup>926</sup>

#### 7.4.2 *The Underlying Doctrinal Socialist Structure of the 1990 Ownership Law*

Developing the detail of the categories set out in the March Constitutional Amendments, article 4 of the 1990 Ownership Law provided for the new “forms of ownership” (ownership of Soviet citizens, collective ownership and state ownership), “mixed forms of ownership”; and left open the possibility for future legislation to provide for “other forms of ownership not provided for by the present law”. In addition it contemplated “common (share or joint) ownership”. The structure of the 1990 Ownership Law reflected these categories containing, among others, sections on the forms of ownership (ie Section II: Ownership by citizens of the USSR; Section III: Collective Ownership; and Section IV: State Ownership); and a section on

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<sup>925</sup> See, generally, *Sotsialisticheskoe Pravovoe Gosudarstvo: Kontseptsiya i Puti Realizatsii* (Yuridicheskaya Literatura:1990).

<sup>926</sup> 1990 Ownership Law, articles 32-34.



certain mixed forms and ownership by "foreign" persons (ie Section V: Ownership of Joint Enterprises and Foreign Citizens, Organisations and States).

This structure was based on the underlying socialist doctrinal regime of "forms of ownership" derived from the identity principle. While the concept of tenures in English land law survived the feudal period to the present day, the continued status of the English crown as *fisc* is almost irrelevant in the practical day-to-day operation of the land law system (other than in the rare instances such as escheat). The legacy of the forms of ownership and the other elements of the "socialist structure" surviving into the 1990 Ownership Law was however quite different and ensured that the possibility of *novostroika* was passed over. It shall be argued that the very retention of this framework, irrespective of the clearly radical change in positive law, was not just lip-service to a vestigial part of an anachronistic regime, but rather served crucially to underpin, distort and obscure the coherence of the new law on ownership itself as well as the development of the law on industrial organisations as consolidated in the 1990 Law on Enterprises.

The retention of this socialist framework in the 1990 Ownership Law meant that the "new" law on ownership continued to be structured by reference to the identity principle without a clear understanding of the mechanism for owning a juridical person, of the nature of the ownership interest of a juridical person and of group structures based thereon. As such, the ownership regime of the 1990 Ownership Law had the effect of drawing artificial links between different organisations, and artificial distinctions between similar organisations, and ultimately meant that the concept of the generic owner and the principles of equivalence, permissive regime and rule of law state, were hijacked and overthrown by the historical socialist tradition of providing different ownership rights for owners with different "identities".

So while the economic constitution of the 1990 Ownership Law contemplated the restructuring and opening up of the economy on the basis of profit, its legal doctrinal structure straightjacketed the development of the juridical person, the subject of this new economy, and condemned its general form to one inherited from the previous Stalin settlement. The juridical person remained tied to the mast of the command system and its theoretical framework, despite the fact that the fundamentals of this economy, based on state ownership and state control of the means of production, had been eroded and replaced by the same law. While the new forms of ownership ensured that the contorted Soviet spine was restructured, the socialist dimension of the underlying doctrinal structure meant that the possibility for the subsequent introduction of the general corporation was lost. Furthermore, the law on industrial



organisations in the Soviet Union in the context of the new regulated market economy became crazed, unprincipled and unsure of a rationale foundation.<sup>927</sup>

#### 7.4.2.1 *The Forms of Ownership Regime - Rationale*

The regime of "forms of ownership" was born from the Soviet economy of the late 1920s and early 1930s shaped by Venediktov's theory of socialist state ownership.<sup>928</sup> It stressed the *identity* of the owner as the overriding determinant of the nature and rights of the juridical person and was formalised in the provisions of the 1936 Stalin Constitution and then in the 1961 FPCivL. Under this legislation, private ownership was abolished, and a "form of ownership" was allocated to certain identified persons and then was used as the basis for the classification of all juridical persons.

While the significance of each particular form of ownership both in the 1961 FPCivL and in the 1990 Ownership Law was considered extensively in Soviet legal literature, the overall concept of the "forms of ownership regime" as a whole (as an alternative to the "generic owner" and a regime for characterising juridical persons by reference to contract and the nature of their ownership interests) was simply accepted at face value. There was broad silence in the literature in Russian as to the rationale for the very framework itself. In western literature sometimes it was noted that the "forms of ownership", set out in the 1936 Stalin Constitution, were imposed by diktat with little theoretical consideration of the distinctions drawn,<sup>929</sup> and at other times, a speculative explanation was offered.<sup>930</sup>

The previous three principal forms of ownership of the 1936 Stalin Constitution (state ownership, cooperative-collective farm ownership and personal ownership) reflected the three basic areas of the economic world at that time, namely industry; agriculture; and the rights of the individual or the collective farm household ("*kolkhozhnyi dvor*"). Throughout the early part of Soviet history, Trotsky's scissors opened and closed to the tune of the different policy

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<sup>927</sup> The implications of the framework of the 1990 Ownership Law for the new constitution of the industrial juridical person is examined infra Section 7.5.

<sup>928</sup> Supra n.57 (1948), Part 2, chapter 9.

<sup>929</sup> For example, Gsovski commented on the 1936 forms that: "Nowhere was a principle stated governing the differences in the status of these categories of ownership. Several overlapping enumerations were given instead." (supra n.22 (1948), p.555).

<sup>930</sup> For example Braginskii, Butler and Rubanov noted of the forms in the 1990 Ownership Law that "the concept of a form of ownership had no precisely determined significance nor precisely established legal consequences. Nor does an analysis of previous legislation offer categorical conclusions". They went on to argue that the status of a form of ownership was given "only [to] that property which...is essential to exist under the conditions in which the Soviet Union lives" (M.I. Braginskii, W.E. Butler, A.A. Rubanov, *The Law on Ownership in the USSR* (Interlist:1991), p.59, 60).



initiatives, first in terms of NEP, the policy of "facing the countryside" and the wager on the kulak; and then in terms of industrialisation and the planned economy, the policy of "favouring" the proletariat coupled with the socialist offensive and collectivisation of agriculture. The legacy of the Tsarist state and the "peasant question" resolved during the struggles for the establishment of a "socialist" economy during the 1920s and 1930s gave rise to a different economic settlement for industry and agriculture. Within agriculture the adoption of the artel form of collective farm gave rise to a different economic settlement as between the collective farm and the old Tsarist household. It has been suggested in this study that the forms of ownership regime developed out of (and hence corresponded to) each of the three key battlegrounds of the emerging Stalin economy of the 1930s; and that they represented an attempt to establish "state ownership" as the general rule and confine the "exceptions" accordingly.<sup>931</sup>

#### *7.4.2.2 The Forms of Ownership Regime and Basic Doctrinal Shortcomings - 1985 to 1990*

As has been argued throughout this study, under traditional Soviet law, the question of the "ownership of" a juridical person (or indeed in relation to any association) was never "satisfactorily" analysed; the distinction between ownership "of" and ownership "by" a juridical person was often never explicitly acknowledged or examined.<sup>932</sup> Indeed, the forms of ownership regime itself sometimes defined the relationship of ownership "of" a juridical person, and sometimes defined the relationship of ownership "by" a juridical person. In short the "success" of the forms of ownership regime relied on an economy where there were a discrete number of owners (defined by reference to the state) and where a specific juridical person could be allocated to each owner on a sole basis; or where the question of "ownership of" a juridical person could simply be overlooked in favour of the concept of "membership". Therefore with regard to the "traditional Soviet juridical persons" (ie state enterprises and collective farms) and the "new juridical persons" (ie joint enterprise and leased enterprises); and the contract-based associations (ie contract for joint activity) the following interpretations can be derived:

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<sup>931</sup> Supra Section 2.3.

<sup>932</sup> This distinction between "ownership of" a juridical person (by another), and "ownership by" a juridical person of property is sometimes further finessed in English language translations of Soviet laws in this area. This is because the genitive case in the Russian language is used when describing "ownership by" a juridical person. For example, the phrase "*sobstvennost' kolkhozov*" means "ownership [of property] by a collective farm", although in Russian "the collective farm" is in the genitive case (and hence is sometimes translated literally as "ownership of a collective farm" which in this context may be misleading and suggest that the meaning of this phrase was "ownership of a collective farm [by another]").



- (a) In the case of the state enterprises (*pre* and *post* 1987 State Enterprise Law):<sup>933</sup>
- (i) Ownership "of" a state enterprise was specified but without careful analysis: the state enterprise was treated as an indivisible entity located entirely in state ownership.
  - (ii) Ownership "by" a state enterprise (or, strictly speaking, its possibility) was of utmost concern to Soviet legal doctrine. State enterprises were conceived as civil law persons separate from the state. Therefore it was considered imperative that they did not have the independent right of ownership as this would otherwise have been considered to have prejudiced the state's monopoly status. The concept of operative management provided an alternative framework. On this basis:
    - (I) it made sense to talk of "property of a state enterprise" (ie allocated to its balance sheet); but that
    - (II) the state enterprise did not have ownership of that property; and hence
    - (III) Soviet law was forced to distinguish between rights (which were not characterised as objects of the right of ownership and hence were capable of being acquired by any juridical person) and property (which was the object of the right of ownership and hence could only be owned by juridical persons with the right of ownership) .
- (b) In the case of the collective farms and the 1988 cooperative enterprises:<sup>934</sup>
- (i) Ownership "of" a collective farm/cooperative enterprise was not even considered directly by the legislation and instead legislation and commentaries focussed on the concept of membership.
  - (ii) Ownership "by" a collective farm/cooperative enterprise was simply governed by the form of collective farm-cooperative ownership.
- (c) In the case of the contract for joint activity: (on the basis that it did not give rise to juridical person):<sup>935</sup>

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<sup>933</sup> Supra Sections 2.3.1, 2.5, 3.4.2, and 6.3.4.3.

<sup>934</sup> Supra Sections 2.4.2 and 6.4.1.

<sup>935</sup> Supra Section 4.6. The juridical status of the contract for joint activity was a matter of some debate (ibid.)



- (i) Ownership "of" the contract for joint activity seemed to be rejected almost by definition as it was not a juridical person.
- (ii) Ownership "by" the contract for joint activity was rejected as it was not a juridical person and hence the participants maintained their rights of ownership to property contributed through the concept of common ownership
- (d) In the case of the joint enterprises: the following analysis has been suggested (although Decree 49 was not very specific on these points):<sup>936</sup>
  - (i) Ownership "of" a joint enterprise as "a juridical person" was rejected in favour of "looking through" the veil of juridical personality, and maintaining the continuing rights of ownership of the participants to property; and as such
  - (ii) Ownership "by" a joint enterprise was rejected and hence its status was similar to that of a state enterprise (ie a juridical person without the right of ownership itself).
- (e) In the case of the leased enterprises:<sup>937</sup>
  - (i) Ownership "of" a leased enterprise by the labour collective (or another person) was entirely unclear as there were no provisions of the FPLease relating directly to this point.
  - (ii) Ownership "by" a leased enterprise seemed to be rejected as it did not fall within any of the existing forms of ownership. However the situation was left unclear due to references to an apparently new form of ownership, collective ownership, that only formally became part of Soviet law following the March Constitutional Amendments.

For each of the above enterprises, the situation was confused following 1988 as Soviet law gradually came to acknowledge the right of each to issue "stocks".<sup>938</sup>

In the Soviet law context, the doctrinal significance of the forms of ownership regime was that it provided the building blocks for a legal system which underpinned the command economy and which distinguished between, and stressed the important differences of, the position of the state in industry (ie direct and monopoly owner of the means of production) and the formal

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<sup>936</sup> Supra Section 5.4.2.

<sup>937</sup> Supra Section 6.5.3.

<sup>938</sup> Supra Sections 6.4.1, 6.5.1 and 6.5.3.1.



legal autonomy of the "peasantry" in agriculture (where collective farms were permitted to own property in their own right).<sup>939</sup> It was perhaps a consequence of these doctrinal imperatives of the forms of ownership regime based on the identity principle that resulted in the following:

- (although often overlooked and as noted above) the forms of ownership meant different things in the context of different juridical persons: in the case of the state enterprise, the forms of ownership regime regulated ownership *of* the state enterprise; whereas in the case of the collective farm/cooperative, the forms of ownership regime regulated the ownership *by* the collective farm/cooperative;
- the question of "ownership of" a juridical person was generally overlooked. The only clear example of an attempt to analyse this question was in the context of the state enterprise which was treated as a single object of the law on ownership with one owner;
- the question of "ownership by" a juridical person gave rise to different regimes for different juridical persons: some had the right of ownership, some did not, and some had an uncertain ownership regime (ie falling within the catch-all category of article 11 of the 1961 FPCivL);
- the presence of juridical persons without the right of ownership gave rise to the distinction between rights and property;

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<sup>939</sup> The main practical consequence of the forms of ownership regime was to provide the basis for limiting the types of assets that each identified "owner" could, or could not, own. However, the limitation of the right of certain persons to own particular assets does not necessitate the doctrinal edifice of the socialist forms of ownership which (as noted above) was more a product of doctrine and history than of practical necessity.

In addition to providing limits on the types of assets a particular person could own, they also had certain implications in the field of criminal law. Soviet criminal law distinguished "Crimes against Socialist Ownership" from "Crimes against Personal Ownership of Citizens" and based on this different severity of punishment (cf 1960 RSFSR CrimC, *Osobennaya Chast'*, chapters 2 and 5). Although this distinction was not made in the original 1926 RSFSR Criminal Code (adopted before the concept of "forms of ownership" had been introduced into Soviet law), the classification and understanding of crimes in terms of forms of ownership was developed in legal doctrine even before the adoption of the new 1960s codes. See, for example, *Kurs Sovetskogo Ugolovnogo Prava, Osobennaya Chast'*, *Tom 1* (Gosudarstvennoe Izdatel'stvo Yuridicheskoi Literatury:1955), parts 4 and 5. The use of criminal law to protect "state property" predated its restatement in civil law in terms of the "forms of ownership" regime. A most extreme example of the application of criminal law to protect state property was the decree of "On the Defence of the Property of State Enterprises, Kolkhozy and Cooperatives and on Strengthening of Social (Socialist) Property" of 7 August 1932 which prescribed the death penalty for theft of kolkhoz property and was interpreted to include grain standing in fields (R.W. Davies, *Crisis and Progress in the Soviet Economy, 1931-1933* (Macmillan:1996), p.242).



- the presence of one type of juridical person for each identified owner on a sole basis enabled the forms of ownership regime to avoid the need to regulate multiple ownership structures and enabled the development of a classification of juridical persons by reference to forms of ownership based on the identity principle; and
- a logical consequence of monopoly ownership by the state and the identity principle was that joint enterprises could not have had the right of ownership (at least in relation to part of its property) because (reasoning from the operative management regime) property contributed to them by the Soviet participant would have had to have remained in state ownership and could not have passed to the ownership of the joint enterprise.

#### 7.4.2.3 *Legacy of the Forms of Ownership Regime in the 1990 Ownership Law*

The *perestroika* economy of the late 1980s was very different from the economy of the 1930s. The Stalin settlement had been fatally undermined by the Gorbachev economic reforms, including most importantly the introduction of owners of the means of production other than the state. Once again a new legal framework was needed and the 1990 Ownership Law defined the new constitution for that new economy.

The possibility of *novostroika* of that economy and the legal characterisation of its actors as suggested in Section 7.2 would have meant an end to the "forms of ownership regime" and an introduction of the concept of the generic owner coupled with a revival of the importance of the nature of the ownership interest. Unfortunately the legislators opted to retain the concept of "forms of ownership" almost on the basis of inertia; and the legal literature of the time, like the legislators, rarely questioned its appropriateness or appreciated its significance when applied in the context of the post-plan economy.

By retaining the importance of the identity principle in the context of this new open economy, the forms of ownership regime by definition precluded a coherent analysis of the juridical person itself (as a generic owner and subject of civil law) and of the ownership interest of that juridical person (as an object of the law on ownership). It neither highlighted, nor adequately regulated, the separate questions of "ownership of" and "ownership by"; and without a clear understanding of the answers to those questions in the context of a law of property based on the generic owner, it is impossible to develop a law of juridical persons for a market economy, with equity capital and group structures based on ownership (rather than administrative) relationships.

In practice, the retention of forms of ownership regime based on the identity principle made little sense, particularly as the open economy now broke the link between an owner and its



related attendant juridical person thereby contemplating the possibility of a juridical person being owned by more than one category of identified owner. Curious distinctions, without any discernible meaning, were therefore created by its continuing application. For example, under the 1990 Ownership Law, ownership of stocks of a joint-stock society by the state was characterised as state ownership; but ownership of those same stocks by a joint-stock society was characterised as collective ownership; and ownership of those same stocks by a citizen was characterised as personal ownership!

By analysing carefully the identification or selection of the "new" persons to be the basis for the "new" forms of ownership of the 1990 Ownership Law, the rationale for their selection can be discerned relatively clearly, as can the ways in which the forms of ownership regime itself inevitably produced a distorted and incoherent framework for the regulation of ownership relations in the open economy:

(a) State ownership:

*Rationale* State ownership seemed to be based on the principles of preserving state ownership as a separate category in its own right and the preservation of the state's direct ownership of the means of production to the extent operated through the state enterprises.

*Regulation* As such, Section IV of the 1990 Ownership Law regulated state ownership separately from other forms; and in order to ensure that state enterprises did not compromise the state ownership principle, the status of state enterprises *without* the right of ownership was retained together with the concept of operative management (coupled with a similar and more devolved framework of "full economic jurisdiction"). State enterprises were therefore also regulated in Section IV as well.

*Relevance/Consequences* The above rationale had little relevance in an open economy, where ownership by the state of a juridical person should have been in principle no different from ownership of that juridical person by any other; and where control over state enterprises should have been no different from control over other juridical persons by their owners (ie through the voting mechanics and other provisions of their charter). The socialist rationale for the existence of a category like "state ownership", and with it the concept of state enterprises (as a subject of civil law but) without the right of ownership, rooted the state industrial organisation firmly within the confirmation governance regime. The possibility of the generic ownership



for all subjects of civil law was therefore precluded due to the fact that there continued to exist a juridical person without the right of ownership.

The presence of a juridical person without the right of ownership further perpetuated the need to distinguish rights (as capable of being acquired by all juridical persons) from property (capable of being owned only by those with the right of ownership). The practical consequences of such a distinction were even uncertain before the *perestroika* reforms: if rights were not "owned", what was the relationship between the holder and the right?<sup>940</sup> It is after all almost impossible to distinguish for these practical purposes between rights and things, between a *chose* and *res*. However in the context of the law of juridical persons in an open economy, it was perhaps even more important for this "meaningless" distinction to be collapsed because the owning of an ownership interest can be based on both the ownership of rights (ie stocks as a bundle of rights) and in some cases on the ownership of property (eg bearer stock) in the Romanist sense.

(b) Collective Ownership / Ownership by citizens:

*Rationale* In order to provide a form of ownership for the new juridical persons and others, and in light of the fact that the old forms of ownership were no longer applicable in the post-Stalin economy, "new" forms of ownership were created.

*Regulation* These seemed to be based on the distinction between the juridical person and the natural person - hence collective ownership and ownership by citizens.

*Relevance/Consequences* While the distinction between natural and legal persons makes sense in the context of distinguishing subjects of *civil law*, it makes little sense in terms of *the law on ownership* - it was wholly unclear what in practice was to be understood by the distinction between ownership by a juridical person and ownership by a natural person. It was almost as if because the forms of ownership regime were to be retained, then, by necessity, different forms "had" to be identified, and the distinction between the juridical person and natural person seemed as convenient as any other. In fact under the very terms of the 1990 Ownership Law itself, there was no conceptual difference between *ownership* by citizens and *ownership* by juridical persons (although of course there is a legal difference between citizens and juridical persons).



In relation to collective ownership, the 1990 Ownership Law provided further separate sub-categories of ownership for different named juridical persons;<sup>941</sup> and there may have been even greater differences between two sub-categories of collective ownership, than between the forms of ownership of citizens and collective ownership.

As regards the law of juridical persons, the distinction between collective ownership and ownership by citizens would have been largely an irrelevance if, as set out in the 1990 Ownership Law, collective ownership in Section III indeed encompassed "ownership by...associations which are juridical persons".<sup>942</sup> Unfortunately not all juridical persons were included within collective ownership - most importantly state enterprises fell outside this form (presumably on the basis that they did not have the right of ownership) and so did joint enterprises (see paragraph (c) below). The fact that certain juridical persons fell outside the scope of collective ownership meant that the 1990 Ownership Law (and the 1990 Law on Enterprises) could still continue the tradition of article 11 of the 1961 FPCivL of classifying and analysing juridical persons by reference to their form of ownership, and by identifying different juridical persons by reference to different owners. Even more so in an open economy, this just resulted in drawing distinctions between juridical persons which in practice were largely irrelevant, and which in doctrinal terms obscured more important issues.

Only if all juridical persons fell within the same category of ownership (whether based on the generic owner or on collective ownership) could Soviet law have been released from the fetters of the forms of ownership structure, and begin to analyse and examine the nature of the juridical person by reference to its "own" characteristics (including its ownership interest) instead of by reference to the identity of its owner.

(c) Ownership by Foreign Persons:

*Rationale* The basis for treating ownership by "foreign" persons separately from ownership by domestic persons seemed to be derived from the traditional Soviet law distinction between foreign trade law and civil law.

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<sup>940</sup> Phases such as "belonging to" suggested that it was "possession" (see supra n.912), but alternatively the nature of the relationship may just have varied depending upon the identity of the right-holder and hence its form of ownership.

<sup>941</sup> Within Section III on collective ownership, there were separate articles respectively on ownership by the leased enterprise, by the collective enterprise, by the cooperative, by the economic society and partnership, by the joint-stock society and by the economic association.

<sup>942</sup> 1990 Ownership Law, article 10(1).



*Regulation* "Ownership of Joint Enterprises, and Foreign Citizens, Organisations and States" was regulated in Section V of the 1990 Ownership Law. This section (separate from the sections on each form of ownership) clearly gave the right of ownership to joint enterprise, foreign citizens, organisations and states. However, this right of ownership existed outside of, and was not given the status of, a form of ownership.

*Relevance/Consequences* Once again, it was unclear what in practice was the significance of distinguishing between the ownership by foreign persons and the ownership by domestic persons. Once again the presence of joint enterprises in Section V further undermined the coherence of collective ownership as the category for regulating the ownership regimes of all juridical persons; and further enabled the continued possibility of classifying juridical persons on the basis of the socialist forms of ownership regime.

It seems that the only sensible rationale for distinguishing the ownership by foreign persons from the ownership by domestic persons was on the basis that the Soviet state wanted to regulate foreign investment specifically. While this is clearly a "legitimate" concern of any state, the regulation of foreign investment could simply have been achieved through stand-alone legislation, without the need to create a new type of juridical person (the joint enterprise). The creation of the joint enterprise as a separate type of juridical person, to be assigned to foreign owners in the pursuit of regulating foreign investment, was simply an extrapolation of the existing logic of the forms of ownership regime based on the identity principle (in the same way that a specific type of juridical person had been assigned to the state as owner (ie state enterprises) and to the peasantry (ie collective farms)).

As a result of regulating ownership by foreign persons (or domestic Soviet persons with foreign participants) separately from ownership by Soviet persons, the classification of juridical persons became bifurcated between specific types of juridical person that had foreign owners and specific types of juridical person that had domestic owners.

#### *7.4.2.4 The Problem of Mixed Ownership*

Certain fundamental practical consequences for the law on industrial organisations generally, and in particular for the analysis of a juridical person with multiple owners, resulted from the "historical difficulties" associated with the forms of ownership regime (as noted in Section 7.4.2.2) and from the inconsistencies in the application of that regime in the context of the



new forms of ownership (as noted in Section 7.4.2.3). As aforementioned, in the context of traditional Soviet law, there was no need to analyse the ownership of juridical persons by multiple persons: state enterprises were wholly owned by the state; the ownership of collective farms/cooperatives was overlooked in favour of the concept of membership; group structures were based on administrative links and not an ownership relationship; and the relationship between participants without the formation of a juridical person was analysed through the concept of common ownership.

Yet, starting with the joint enterprises and moving through the later expressions of the participation enterprises and beyond, it became clear that the "new" industrial organisations "demanded" a regime for multiple owners where one identified owner may own more than one type of juridical person. In the case of *novostroika* this would have been developed on the basis of the generic owner and the holding of ownership interests of a juridical person without affecting the nature of that juridical person or its underlying ownership regime (due to the distinction between the juridical person and its ownership interest). Unfortunately such an analysis was not possible in the context of the forms of ownership regime; and under that regime the only precedent for analysing "ownership of" a juridical person was the case of the state enterprise: the state enterprise was treated as an indivisible object of the law on ownership, with a single owner, and with an ownership regime characterised by reference to that single owner based on operative management.

The multiple owners problem most specifically questioned the basic principles of conceiving of the juridical person as an indivisible object and of defining the regime of ownership *by* a juridical person in terms of the identity *of* the owner of that juridical person. Put in general terms:

- if a juridical person was to have the right of ownership, would this right of ownership be affected if the identity of the owner of that juridical person changed? and
- how would this ownership regime be analysed in the context of multiple owners?

Or to pose this issue in terms of an example: under the 1990 Ownership Law, the joint-stock society by definition issued ownership interests (stocks) and was given the right of collective ownership; however:

- what would the legal analysis be if (all its stocks) became wholly owned by the state? would that mean that the joint-stock society lost its right of ownership (like the state enterprise) and be analysed as an indivisible object of state ownership?



- what would be the legal analysis if its stocks were partly owned by the state and partly owned by a Soviet domestic cooperative?
- what would be the legal analysis if part of its stocks were owned by a foreign person?

Such questions would have been almost trivial in the context of *novostroika* and a law of property based on the generic owner. However in the context of a regime based on forms of ownership, these questions posed critical problems which the forms of ownership regime simply did not have the legal tools to solve - for no solution could have been found without a full understanding of the distinction between ownership *of* and ownership *by*, and of the nature of the ownership interest.

In struggling to find a solution to the question of analysing the issue of "ownership of" a juridical person with multiple owners, the 1990 Ownership Law provided for the concept of "mixed ownership" (as separate from "common ownership"). Article 4(2) of the 1990 Ownership Law provided that "the combining of property owned by citizens, juridical persons and the state, and the formation of mixed ownership on this basis, including the ownership of joint enterprises with Soviet juridical persons and foreign juridical persons and citizens, shall be permitted".

It is important to note that "property owned by...juridical persons" as mentioned in article 4(2) was not synonymous with collective ownership due to the fact that collective ownership did not regulate the ownership by all juridical persons (most notably the ownership regimes of state enterprises and joint enterprises did not fall within collective ownership). Therefore, article 4(2) implicitly abandoned the forms of ownership distinctions (ownership of citizens, collective ownership and state ownership) for more generic civil law categories based on the property of the citizens, juridical persons and the state, without an explicit distinction between domestic and foreign persons.

As regards the application of "mixed ownership" to ownership between domestic owners falling within different categories of ownership (eg the ownership of stocks in a joint stock society by the state and by a cooperative), article 4(2) did not provide any details of the mechanism by which this multiple ownership structure would be achieved or the doctrinal effect that this would have. Presumably the object of this multiple ownership structure would depend upon the relevant ownership interests (if any) of the particular juridical person in question. However the juridical effect of this mixing of forms of ownership was not specified; and as such there was no indication as to how the questions posed above would be analysed. To adopt a Dworkinian expression, it seems as if at this point the rules based on the forms of



ownership regime simply "ran out". However, in relation to mixed ownership between a Soviet and a foreign person, the 1990 Ownership Law did provide further guidance.

The mixing of ownership between Soviet and foreign juridical persons was analysed by reference to the concept of the joint enterprise in the 1990 Ownership Law. Article 27 adopted a "new" definition of the joint enterprise as follows: "joint enterprises with the participation of Soviet juridical persons and foreign juridical persons and citizens...[are] created on the territory of the USSR in the form of joint stock societies, economic societies and partnerships". Previously a "joint enterprise" had been simply a juridical person established pursuant to Decree 49. Article 27 by contrast contemplated a wider definition of the "joint enterprise", encompassing for example joint stock societies with foreign participation. Again by contrast to Decree 49 joint enterprises, the article 27 joint enterprise, as mentioned above, was given a right of ownership (regulated by Section V of the 1990 Ownership Law), separate from collective ownership (regulated by Section III of the 1990 Ownership Law).

Therefore, while it was unclear in the domestic context whether, for example, mixed ownership between the state and a domestic juridical person of a joint stock society would effect the juridical status of the joint stock society, it seemed that the mixing of ownership between domestic and foreign juridical persons of a joint stock society, would "transform" that joint stock society into an article 27 "joint enterprise" with a different ownership regime. This approach had a precedent in the transformation of the organisation of lessees into the leased enterprise following the execution of the lease contract; and was based on a similar rationale.<sup>943</sup>

However even in the context of mixed ownership between domestic and foreign persons, the new article 27 definition of the joint enterprise presented a number of further issues because the definition:

- did not include foreign participation in all Soviet juridical persons, but only in "joint stock societies, economic societies and partnerships". In particular, participation in Decree 49 joint enterprises was not specifically mentioned (though clearly intended to be covered by Section V) and notably absent were cooperatives and social organisations;
- did not permit participants to be Soviet citizens; and
- did not contemplate enterprises wholly owned by foreign participants.

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<sup>943</sup>

Supra Section 6.5.2.2.



The regulation of each of these situations was simply left unanswered thereby rendering moot the questions posed at the beginning of this Section in this regard.

In summary, in the pursuit of the seemingly simple task of providing for the legal regulation of multiple ownership and foreign investment, the logic of the forms of ownership regime resulted in an initial framework that (i) set out "forms of ownership"; and (ii) then elaborated the types of juridical person by reference to the identity of their owners (based "broadly" on civil law subjects), and (iii) therefore implied that where the owners of a juridical person changed or became mixed, the form of ownership of that juridical person changed as did the nature of the juridical person itself. While the rationale for mixed ownership concept as a product of the doctrinal imperatives of the forms of ownership regime is relatively clear, its exposition in the 1990 Ownership Law was thoroughly incomplete, and its legal consequences in practice were simply unintelligible.

#### 7.4.3 *Summary and Outstanding Issues*

There were certain references in the 1990 Ownership Law which were clearly derived from the previous socialist regime. The best example was the statement in article 1(6) that the "use of any form of ownership must preclude the alienation of the worker from the means of production and the exploitation of man by man". These references were generally understood at the time to be discrete examples of lip-service to an *ancien regime*. Overall the 1990 Ownership Law presented a coherent and radical structure for the development of market economic relations. In this Section it has been argued that in fact, far from being isolated examples, articles such as article 1(6) were a reflection of a deeper underlying doctrinal structure based on socialist principles and most importantly on the retention of the "forms of ownership regime" based on the identity principle.

The concept of forms of ownership rendered the generic definition of "the owner" in article 1 as hollow. The "new" ownership regime continued to be structured by reference to the identity principle despite the fact that the Stalin economic settlement, which had given rise to that principle, had firmly been overthrown by the Gorbachev reforms. In the context of a market orientated economy, there was no way to distinguish meaningfully different "identities" to be used as the basis for the new forms of ownership, and, "broadly" the selection of the categories of the natural person, the juridical person and the state was inevitably going to be problematic, particularly because not all Soviet juridical persons were regulated by "collective ownership".



While the 1990 Ownership Law set out the legal regime for the "new" economic framework, the 1990 Law on Enterprises developed that framework in elaborating the new constitution for the "new" industrial juridical person. The basic precondition for the development of the general corporation as set out in Section 7.2 (ie the development of the generic owner) had been overlooked in favour of the continued application of forms of ownership regime and the identity principle. It was from within that framework that the 1990 Law on Enterprises tackled the other preconditions: namely the separation of ownership from control and the concept of equity capital, a complex management regime, an understanding of the property rights of the participants and the right to incorporate.

## 7.5 1990 Law on Enterprises

The then current definition of the juridical person appeared in article 11 of the 1961 FPCivL which used the term "organisation". The industrial "enterprise" was referred to in article 11 as one type of juridical person or organisation which was state owned and operated on the basis of *khozraschet* within the industrial economy. It has been argued that it is best understood within the confirmation model. The legislation relating to the contract-based concession enterprise and each of the participation enterprises also adopted the term "enterprise" to describe the relevant juridical person,<sup>944</sup> but it was uncertain at that time whether anything turned on this use of terminology.

Although it was never explicitly stated as a purpose of the 1990 Law on Enterprises in the preamble (nor explicitly recognised in most of textbooks and commentaries), the Law on Enterprises contained an implicit categorisation because this law did not regulate all juridical persons. The "choice" of juridical persons falling within its scope (and hence within the definition of "enterprise") was not made on the basis of "forms of ownership" because the Law on Enterprises was expressed to apply to "enterprises under diverse forms of ownership". From its scope, it seems as if the Law on Enterprises was developed in order to regulate all juridical persons operating within the industrial economy both commercial and non-commercial. It therefore did not regulate juridical persons of the administrative state nor did it cover state farms or collective farms. As such, it shall be argued that the Law on Enterprises primarily provided a new constitution for the *industrial* organisation.

Although "organisation" was used in article 11 for the generic juridical person, the law was expressed to be "on Enterprises" and not "on industrial organisations" or "on industrial juridical persons" generally; and it shall be argued that this was quite deliberate, significant

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<sup>944</sup> Namely the joint enterprise, the 1987 state enterprise, the cooperative enterprise and leased enterprise.



and appropriate. The new constitution of the industrial juridical person was founded upon the underlying socialist framework of the 1990 Ownership Law, and ultimately on the previous socialist state enterprise. As such, the 1990 Law on Enterprises failed to introduce any of the remaining preconditions to the introduction of the general corporation as contemplated in Section 7.2 above; and indeed constructed a regime that was deeply indebted to the confirmation model. For this reason, the title of the 1990 Law on Enterprises was well chosen. As the 1990 Ownership Law maintained an underlying socialist framework in the "new" economic constitution, it shall be argued that the 1990 Law on Enterprises truly represented the triumph of the socialist "enterprise" over the general corporate form.

#### 7.5.1 *The Concept of the Generic Enterprise and Classification of Enterprises*

The "enterprise" was defined in article 1 of the 1990 Law on Enterprises as "an autonomous economic subject with the rights of a juridical person which on the basis of the use of property by the labour collective produces and realises a product, fulfils work and renders services. An enterprise, shall not have other juridical persons as a part thereof...[and], irrespective of the form of ownership of the means of production and other property, shall operate on the principles of *khozraschet*". This definition therefore set out the general description of the industrial organisation and appeared to be broadly uncontroversial. It was clearly intended to embrace all "enterprises under the diverse forms of ownership".<sup>945</sup> Thus the state was directed to "ensure an enterprise, irrespective of the forms of ownership, equal legal and economic conditions for economic activity".<sup>946</sup>

Unfortunately this definition, like that of the generic owner, was then distorted by imposing a classification on these enterprises that was indebted to the forms of ownership regime adopted by the 1990 Ownership Law. Hence article 2 of the 1990 Law on Enterprises classified "enterprises" as follows:

- (a) Those based on ownership by Soviet citizens: individual and family enterprises;
- (b) Those based on collective ownership: collective enterprise, production cooperative; enterprise belonging to a cooperative; enterprise created in the form of joint-stock societies or other economic societies or partnerships; enterprise of a social organisation or religious organisation; and

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<sup>945</sup> 1990 Law on Enterprises, preamble; see also article 4(1) ("state enterprises...and enterprises of other forms of ownership shall be guided by the present Law...").

<sup>946</sup> 1990 Law on Enterprises, article 31(1).



- (c) Those based on state ownership: State union enterprise, State republic enterprise and enterprises of other administrative sub-divisions of the Soviet state.

To this classification were added three additional provisions: (a) joint enterprises could be created by Soviet juridical persons and foreign juridical persons or foreign citizens; (b) any enterprise, depending upon its size, could be designated a "small" enterprise (and hence subject to a special regime); and (c) other enterprises could also operate, including leased, provided that their creation was not contrary to legislative acts of the USSR.

The 1990 Law on Enterprises built upon the doctrinal socialist structure of the 1990 Ownership Law and retained the method of classification that had been inherent in article 11 of the 1961 FPCivL, namely by reference to forms of ownership. The shortcomings of a classification based on forms of ownership has been discussed in some length in Section 7.4.2. As has been argued, the retention of the framework of forms of ownership itself made little sense within the context of an open economy, and furthermore there was no reason for distinguishing different ownership regimes on the basis of subjects of civil law. Most importantly it obscured a proper understanding of the juridical person as a subject of civil law and of its "ownership interests" as an object of civil law; and in particular the socialist framework resulted in distinguishing of state enterprises and foreign owned juridical persons as distinct from other juridical persons and did not provide a satisfactory legal regime for regulating multiple owners.

The classification in article 2 was problematic for two particular reasons:

First, it did not consistently apply the distinction between ownership of and ownership by a juridical person, and hence perpetuated the lack of clarity concerning these two critical and basic concepts. This lack of consistency was surely the result of an incomplete understanding of the basic framework of ownership interests and juridical persons obscured by the shadows of the forms of ownership regime. The nature of the inconsistency can be traced to the basic doctrinal shortcomings of the traditional forms of ownership regime. Therefore the first and the last categories (ownership by citizens and state ownership) in this classification listed juridical persons by reference to the identity of their owners. Obviously it was unclear even then whether only citizens could have owned individual or family enterprises, but it must be assumed that this was the case. However the second category (collective ownership) in this classification seemed to be based on the ownership regime governing the ownership *by* the juridical person, without reference to the identity of its owners. Once again, by incorporating the inconsistencies at the heart of the forms of ownership regime, it seemed that the new



legislation stepped back from dealing with the most fundamental challenge posed by the new industrial organisations, that of regulating multiple ownership structures.

Secondly and more discretely, in contrast to the position under the 1989 FPLease and 1990 Ownership Law which applied the collective ownership regime, the leased enterprise was placed in the "catch-all category" of the classification regime of the 1990 Law on Enterprises (and not within collective ownership).

The retention of the socialist framework for the basic classification of "enterprises" and the rejection of the nature of the ownership interest as a keystone concept informed the detail of the law in each of its most important areas:

- The 1990 Law on Enterprises took a broader concept of the role of the enterprise as a vehicle for fulfilling the interests of the state, employees and owners (thereby eschewing a narrower understanding of the enterprise as a vehicle for the elaboration in the first instance of the interests of the owners of its ownership interests);
- This meant that the governance regime was constructed to align the interests of the state, workers and owners (and not on the basis of the separation of ownership from control, and the alignment of the interests of managers with those of the owners that had appointed them);
- The orientation on wider interests and the doctrinal position of the 1990 Ownership Law meant that the law failed to regulate adequately the ownership of, and the ownership by, an enterprise and hence to distinguish properly between the property of the owners of the enterprise and the property of the enterprise itself; and
- Finally, while expressing the principles of equivalence, the permissive regime and the rule of law, the 1990 Law on Enterprises continued to contemplate a developed role for the state, in what the law called, a "regulated" market which ultimately precluded the permissive regime giving rise to a permissive procedure for "incorporation".

This law applied to all enterprises already existing under Soviet law including the contract-based concession and participation enterprises as well as to the new juridical persons whose introduction was clearly imminent (such as the joint stock society and partnership). Each of the above elements of the 1990 Law on Enterprises therefore ensured that these "enterprises", irrespective of their type, were distinctly socialist in their doctrinal structure; and although the law included cooperatives and joint-stock societies specifically within its ambit, it meant that



all of these enterprises were very different from the "general corporation" of a market economy.

### 7.5.2 *The Role of the Enterprise*

Article 1(2) of the 1990 Law on Enterprises set out the "principal tasks of the enterprise". They were listed in the following order: (a) "the satisfaction of social needs"; (b) "the realisation of social and economic interests of the members of the labour collective" and (c) "the interests of the owner". The traditional "general corporation" is conceived more narrowly, first in terms of a vehicle for the expression of the interests of its owners, and hence the principal governance question relates to the balancing of the interests of different owners and then how to ensure that their appointed managers act in those interests. By classifying the enterprise by reference to forms of ownership and by expressing its role first in terms of satisfying "social needs", then in terms of protecting the interests of the labour collective and finally in terms of expressing the interests of the owners, the 1990 enterprises, irrespective of type, were firmly wedded to a social (or socialist) orientation.

This orientation was given expression through legislative diktat and informed not only the detail of the management structure and the socialist structure of the ownership regime, but also the direction of their required planning activities,<sup>947</sup> the choice of their activities,<sup>948</sup> and their role in wider social services including the support of "medical, children's, cultural-enlightenment, instructional and sport institutions...public dining...and organisations servicing the labour collective".<sup>949</sup>

The expanded role of the enterprise had its roots in the logic of the planned economy and the early days of Soviet industrialisation. "Trusts" and "enterprises" in the planned economy were not run on the basis of profit but on the basis of the plan and during the late 1920s were conceived as institutions that were responsible for feeding, housing and clothing its workforce.<sup>950</sup> In this spirit of the late 1920s, the Soviet "enterprise" was born, developed

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<sup>947</sup> "An enterprise shall independently plan its activities...to ensure the production and social development of the enterprise and raise the personal incomes of its workers...[and] shall [take into account] when preparing plans...ecological, social, demographic and other consequences affecting the interests of the population of the territory" (1990 Law on Enterprises, article 23).

<sup>948</sup> "In its activities an enterprise shall take into account the interests of the consumer and his requirements for quality of the product, work or service" (1990 Law on Enterprises, article 24(3)).

<sup>949</sup> 1990 Law on Enterprises, article 29(6).

<sup>950</sup> Indeed the 1927 Trusts Statute specifically contemplated a "fund for the improving of the living conditions of workers and employees" to which 10% of the net profit was required to be allocated (article 43 and 46(a)). In addition the so-called "director's fund" was created pursuant to the STO decree of 14 June 1928 which provided that following a saving in production costs, 25-50% of the saving could be



through the confirmation model, and persisted through into this new constitution for the generic industrial enterprise of the 1990s.

In certain respects the "enterprise" of the 1990 Law on Enterprises clearly moved beyond that of the "confirmation" Soviet enterprises. For example the state was no longer the sole owner and profit was to be the indicator of its efficacy. However, like the legal framework of the "new" ownership regime which overlooked new economic realities in the embrace of the socialist forms of ownership, the 1990 enterprises still were conceived within the confirmation model more generally. Faced with the option of *novostroika* in March 1990, the Soviet state found it impossible finally to cut the enterprise loose to sail upon the seas of the market. There was no faith in the "hidden hand" to ensure a wider social or ethical dimension. Instead, the Soviet state, clinging to the traditional methods, required, by legislative diktat in the 1990 Law on Enterprises, that all enterprises should continue to maintain an express and explicit wider role in the fulfilment of social needs and those of the labour collective, even in precedence to those of its owners.

### 7.5.3 *Management and Governance*

Section IV of the 1990 Law on Enterprises was entitled "Management of the Enterprise and Self-Management". It contemplated various interest groups, management organs and positions. The internal structure broadly comprised:

- the owner,
- the director of the enterprise and the deputy directors of the enterprise and directors of its structural subdivisions,
- the council (board) of the enterprise, and
- the labour collective of enterprise and the general meeting (or conference) of the labour collective of the enterprise.

Developing the role of the enterprise as set out in article 1(2), the management structure was crafted with the aim of "combining the principles of self-management of the labour collective and the rights of an owner".<sup>951</sup> The overriding importance of the labour collective was suggested by the fact that the articles relating to its role in the management structure were set out in Section IV before those articles dealing with the role of the board and the director. This

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credited to a director's fund to be used again for improving the living conditions of workers and employees.

<sup>951</sup> 1990 Law on Enterprises, article 14(1).



suggested a more active role of the labour collective along the lines of the first expression of the participation model. However, the substance of Section IV as a whole proved that, notwithstanding this ordering of articles, the basic management structure of the 1990 enterprises followed closely that of the traditional state confirmation enterprise.

An acknowledgement of the existence of multiple owners with different separate interests was broadly absent from the provisions of the 1990 Law on Enterprises. It was almost assumed in the drafting that every enterprise had only *one* owner. There was no treatment of how the interests of different owners might be reconciled and there was no contemplation of a general meeting of owners or other such organ which had exclusive competences to make decisions at this level.<sup>952</sup> Indeed, with the exception of article 5(1) which referred to a "decision of the owner (owners)", in all places in the 1990 Law on Enterprises the singular form, "owner" ("*sobstvennik*") was used.

The 1990 Law on Enterprises went on to provide that "the owner shall effectuate his rights with regard to the management directly or through organs empowered by him".<sup>953</sup> Two possibilities were therefore presented: the owner could act as the executive organ (such as in the case of enterprises based on personal participation) or could appoint representatives to the board (such as in the case of the state enterprise where the owner was the state).

Article 14(2) provided that "the hiring...of the director of an enterprise shall be the right of the owner". The director was the delegate of the owner and was expressed to have the power to decide independently all questions not delegated to the general meeting of the labour collective or the board. His powers generally included the right to act without a power of attorney in the name of the enterprise, sell assets of the enterprise, issue orders and give binding instructions on the workers of the enterprise.<sup>954</sup> Deputy directors (appointed by the director) and single directors for each structural subdivision were also contemplated. This replicated the framework of one-man management.

In addition to the director, the owner had the right to appoint representatives to the board headed by a chairman elected from its members. The law set out various matters that were within the competence of the board (although it failed to specify whether this competence was exclusive or could not be altered by the provisions of the charter). These included deciding the general orientation of economic and social activities of the enterprise, the procedure for

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<sup>952</sup> Article 14(2) mentioned the election of the director thereby implying that a collegial organ at the level of the owner must have been considered.

<sup>953</sup> 1990 Law on Enterprises, article 14(1).

<sup>954</sup> 1990 Law on Enterprises, article 19.



distribution of net profit and, upon the recommendation of the director, the issuance of securities of the enterprise. The 1990 Law on Enterprises provided that the board should consist of equal numbers of representatives "appointed by the owner...and elected by its labour collective, *unless provided otherwise by the charter of the enterprise*".<sup>955</sup> The proviso clearly enabled the possibility of disenfranchising the rights of the labour collective.

The labour collective comprised all workers of the enterprise and they participated in the general meeting or conference of the labour collective which appointed the board representatives of the labour collective and dealt with matters relating to the collective contract. Various other rights were given to the labour collective or its conference including: the right to purchase or lease the enterprise,<sup>956</sup> the right to be allocated stocks and other securities of the enterprise,<sup>957</sup> and the right to participate in social and economic questions,<sup>958</sup>

The reference to a single owner and a single director was clearly indebted to the confirmation model. The management structure only hinted at the possibility of multiple owners and the possibility of a collegial management organ which did not sit comfortably with the notion of a single director/manager. In short, the provisions applied most readily to the "state enterprise" and were no doubt born of the socialist orientation of the 1990 Ownership Law. The notion that all enterprises regulated by the 1990 Law on Enterprises should have adopted such a management regime not only contradicted the existing legislation for the contract-based concession and participation enterprises (as well as future legislation) but also betrayed the extent to which legislators wished to construct the new enterprises of the *perestroika* era upon traditional socialist doctrinal principles. There was also deep reluctance to construct a generally applicable governance regime upon the notion of multiple owners and an enterprise as a vehicle primarily for the pursuit of the owners' interests. Furthermore, quite apart from any question of principle, the detail of the law relating to the composition, competences and procedures of each internal organ or position was entirely inadequate. These new enterprises were entirely novel for a whole generation of Soviet citizens and in such an economy, clear, detailed and precise legislation was critical. Its absence merely further indicated a further

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<sup>955</sup> 1990 Law on Enterprises, article 18(1) [emphasis added].

<sup>956</sup> The possibility of purchasing the enterprise set out in article 5 and also provided for by article 12 of the 1990 Ownership Law was again an indication of the possibility for privatisation.

<sup>957</sup> This is considered in more detail *infra* Section 7.5.4.1.

<sup>958</sup> 1990 Law on Enterprises, articles 14(3) and 29.



desire on the part of the state to continue to use the ambiguities of law to exploit control through non-legal mechanisms.

#### 7.5.4 *The Ownership Regime and Responsibility*

Taking into account the role of the enterprise as set out in the 1990 Law on Enterprises and the problematic framework of the 1990 Ownership Law, it is perhaps unsurprising that the law failed to provide a clear and coherent footing for the most critical element of the new juridical person - the ownership regime. The provisions of the 1990 Law on Enterprise in this respect were not only based on the socialist forms of ownership as set out in the 1990 Ownership Law but they continued to finesse the understanding of the ownership interest of a juridical person as an object of the right of ownership, and the juridical person itself as the subject of the right of ownership/civil law. Hence the law maintained the general confusion between the concepts of "ownership of a juridical person by its owners" and "ownership by that juridical person".

##### 7.5.4.1 *The Property of the Owners and the Property of the Enterprise*

As has been discussed, the concept of "the nature of an ownership interest" was absent from orthodox Soviet law. As the Soviet state was the *sole* owner of *all* enterprises, the legislation simply provided that state enterprises belonged to the state, located within state ownership. With the development of the contract-based concession and participation models, the relevant legislation was forced to consider at some level of detail the nature of the ownership interests of the participants. Any interpretation or analysis of any enterprise with multiple owners in the post-command economy should have acknowledged the distinction between the ownership *of* the enterprise (through an understanding of ownership interests of the enterprise, and the rights that the owners acquired by virtue of their ownership of such interests) and the ownership *by* that enterprise of property.

The 1990 Ownership Law failed to take up the challenge to develop a new law on ownership based on the generic owner and by reference to the nature of different ownership interests in different juridical persons and the different rights that therefore accrued to the owners thereof. Instead, the 1990 Ownership Law constructed its "new" framework based on the traditional socialist concept of "forms of ownership" and the importance of the identity of the owner, retaining the possibility for the continued application of operative management. Predictably therefore the 1990 Law on Enterprise did not contain any provisions setting out an understanding of the place and nature of the ownership interest of any owner, despite being required to take into account certain ownership interests by virtue of their clear presence, such



as the stock. It will be argued that the terminology used was hopelessly confused and the concepts so rudimentary that any meaningful understanding was lost.

First, the 1990 Law on Enterprises used the term "owner" and "founder" almost interchangeably.<sup>959</sup>

Secondly, as already noted, there was no clear acknowledgement of multiple owners. With few exceptions, the law invariably referred simply to "the owner" (singular).

Thirdly, the law always referred not to the owner "of the relevant ownership interest of the enterprise" (eg the owner of the stocks of the enterprise) but instead to the "owner of the property of the enterprise".<sup>960</sup> This evidenced again the profound misunderstanding of the nature of the owner-enterprise relationship in an open economy and suggested a failure to move beyond the confirmation / operative management regime where the owner of the enterprise (ie the state) was also the owner of its property.

In fact under the existing 1990 Ownership Law, the only way that the owner of a juridical person could have been "the owner of the property of the enterprise" was within the regimes of "operative management" and "full economic jurisdiction" and these only applied in the case of state enterprises. As such, for all other enterprises, the use of the phrase "owner of the property of the enterprise" simply was wrong. Indeed both the 1990 Ownership Law and the 1990 Law on Enterprises explicitly contemplated that "property of an enterprise may...belong to it by right of ownership...".<sup>961</sup> This inevitably meant that there must have been occasions where the owner of the enterprise was not the "owner of the property of the enterprise".

In any event, the phrase "owner of the property of the enterprise" was used constantly throughout the law and it simply betrayed a fundamental misunderstanding of the concepts of the ownership of the enterprise and the nature of equity capital, each of which were fundamental for the emergence of a general corporate law from the shadows and opacity of the socialist enterprise law.

This confused understanding and drafting was then applied in the context of what few references there were to the concept of ownership interests. The 1990 Law on Enterprises

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<sup>959</sup> Article 5(1) referred to the enterprise created by decision "of the owner", where the word founder would have been more appropriate; and article 10(3) mentioned property of the enterprise to include "cash and material contributions of the founders", whereas the term owner may have been more appropriate and thereby contemplated the possible issue of further ownership interests (eg stocks) after the creation of the enterprise.

<sup>960</sup> For example, articles 1(2), 5(2), 14(2) and 18(1).

<sup>961</sup> 1990 Law on Enterprises, article 10(2).



only mentioned the concept of ownership interests almost by default in its treatment of the "fees" ("vznos") of the founder; the issue of securities ("tsennye bumagy"), and the "contributions" ("vklad") and fees ("vznos") of the labour collective.

Article 10(3) included "cash and material fees ("vznos") of the founders" as one of the "sources for the formation of property of the enterprise". This phrase was ambiguous as it is unclear what the word "fee" was intended to mean - either it could have been interpreted as consideration for the purchase by the founder of ownership interests issued by the enterprise; or alternatively it could have been interpreted as property "contributed" to the enterprise but remaining in the ownership of the founders (which would have been consistent with the phrase "owner of the property of the enterprise"). The use of the word "founder" (rather than "owner") in this context was also perhaps misleading because it suggested that "fees" were only contributed on creation of the enterprise and not at any other time.

Ownership interests were next mentioned in the 1990 Law on Enterprise in the context of "securities". As already mentioned, the Russian term used for securities, "tsennye bumagy", includes both debt and equity securities (ie stocks). Article 12 of the law provided the general rule that "in order to attract additional cash assets...an enterprise shall have the right to issue and realise securities" and article 18 gave the right to issue securities to the board of the enterprise upon the recommendation of the director.

The reference to "securities" was either an example of inappropriate drafting intended to be used only to refer to debt securities; or alternatively, it might have been assumed at the time that *any* enterprise could have issued stocks and it was not understood that in contrast to debt securities, stocks conferred an equity interest. In view of the general socialist orientation of the legislation and the clear existing confusion over the precise nature of ownership interests and equity capital, and in light of the explicit reference to stocks in article 21(3) (discussed below), the reference to "securities" in article 12 was probably more likely to have been on the basis of the latter interpretation and evidenced a total misunderstanding of the concept of the equity interest.

An understanding of the nature of "fees" and of "securities" was confused further by the provisions relating to the distribution of profit and the rights of the labour collective in article 21(3). Article 21(3) provided that in specified instances "part of the net profit shall be transferred to the ownership of members of the labour collective...The amount of profit belonging to a member of the labour collective shall form his contribution ("vklad"). Stocks may be issued in the amount of the contribution to the member of the labour collective. An enterprise annually shall pay interest (or dividends) to the member of the labour collective...".



Article 39 provided further, that in the case of liquidation, this contribution would be returned to the member in advance of payments made to owners. These provisions reproduced almost verbatim the provisions of article 25 of the 1990 Ownership Law. This terminology was further confused by the drafting of article 27(1) which referred to "the sale of securities, share ("paevye") and other fees ("vznosy") of members of the labour collective".

The drafting of article 21(3) illustrated most readily the confusion in the approach of the legislators and the inadequacy of basic understandings in relation to the fundamental question of equity and the nature of the ownership interest. First article 21(3) used the word "stocks" (not "securities" (which may have been debt or equity)) and then contemplated a payment of "interest" on them.<sup>962</sup> Secondly, it again assumed that any enterprise could issue stocks. Thirdly, it was unclear whether there was any difference between the terms "contribution" used in articles 21(3) and 39 and "fee" and "share" used in article 27(1). Finally, it was unclear whether the rationale of article 21(3) was only to provide a financial incentive for workers. If so, the use of the term "stocks" (as opposed to "bonds" or other securities) was obviously erroneous as stocks generally carried with them additional rights to be involved in management.

The use of various terms to describe ownership interests throughout the legislation of the *perestroika* period was simply nonsensical. This dated to the early attempts to use this terminology in the context of the contract-based concession model,<sup>963</sup> and then the treatment of the right to issue stocks and other securities in the context of the second expression of the participation model.<sup>964</sup> The 1990 Law on Enterprises simply continued what had always been a vain attempt to create coherence from within a framework inadequate to deal with such post-socialist concepts.

In summary, the use of the terms "owners of the property of the enterprise" and the confused use of the terms "fees", "securities", "stocks", "contributions" and "shares" betrayed the fact that the forms of ownership regime and the legacy confirmation model had successfully obscured a proper understanding of the ownership regime of the enterprise and in particular the rights of the owners and the nature of the ownership interests. In this context the emergence of a general corporate model was not likely or even possible.

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<sup>962</sup> Curiously article 25(2) of the 1990 Ownership Law were clearer on this point as it referred to the payment of "interest (or dividends) on the contribution (or stock)", suggesting two different forms of "investing" the profit share of the labour collective member by debt or equity.

<sup>963</sup> Supra Section 5.4.2.1.

<sup>964</sup> Supra Section 6.4.1, 6.5.1 and 6.5.2.1.



#### 7.5.4.2 *Associations and Subsidiaries*

The emphasis on forms of ownership and the lack of clear drafting on the crucial point of the nature of the ownership interest almost inevitably meant that the provisions dealing with group structures in the 1990 Law on Enterprises continued to be steeped in socialist understandings.

As has been outlined, traditionally the concept of the "association" under Soviet law was based on administrative governance techniques.<sup>965</sup> The association was an abstraction, coordinating the activities of the enterprises that had acceded to it. However in legal terms, the association and the enterprises were separate juridical persons (both owned by the state and not by each other) and therefore control by the former over the latter was effected by way of administrative instruction and not by way of an ownership relationship (such as voting rights). Such a curious structure from a legal point of view was only possible in an economy where the state owned exclusively all the enterprises and all the associations, where there was no practical necessity to distinguish between ownership relationships and administrative governance mechanisms. However in the new Soviet economy where the state had ceded its monopoly position over the means of production to other actors, a more "ownership" based law of group structures should have evolved where one juridical person controlled another only by virtue of the rights that it received as a result of the ownership of the relevant ownership interests of the other (eg as a result of its stockholding). The regulation of groups in the 1990 Law on Enterprises was founded broadly upon this traditional Soviet framework. However there was evidence in specific areas of a drift towards a more market economy understanding of group structures.

The law retained the concept of the "association" but attempted to put it on a more permissive footing.<sup>966</sup> The association was defined as an independent juridical person with its own balance sheet created for the purpose of co-ordinating activities and representing the common interests of its enterprises. The law then stressed the fact that the association could only be created on a voluntary basis, with a charter confirmed by its founders, and that the constituent enterprises had the right to withdraw. Although this new regime remodelled the association on a voluntary basis, the essence of its structure was still that of the Soviet model. The association was not (and was traditionally not intended to be conceived of as) a holding company to which the ownership interests of its constituent enterprises were transferred. Indeed such a characterisation would have legally precluded the right of a constituent enterprise to withdraw from the association. The governance regimes of these associations could still only be based

<sup>965</sup> Supra Section 6.5.1.

<sup>966</sup> 1990 Law on Enterprises, article 3.



on administrative relationships (akin to planning instructions issued by the state). It was unclear how the association would operate where its constituent enterprises were not exclusively state enterprises and more precisely what was to be the ownership or legal relationship between the association and such enterprises. This might have developed on the basis of contract.

In addition to the "association", the 1990 Law on Enterprises also referred to "unions, economic combinations, concerns and other associations", as well as to "branches, representations, divisions and other solitary subdivisions" and further to "structural subdivisions (entities, shops, sections, divisions, sectors, farms, and other analogous subdivisions of an enterprise or structural entity of an association)".<sup>967</sup> Traditionally, as discussed in Section 6.5.1, the three principal terms used within the Soviet law on groups were the association, the branch and the representation; however it was not uncommon for various other terms such as those used in the 1990 Law on Enterprises also to be used in the legislation without a precise legal meaning. The plethora of terminology in this area, without clear distinctions between any terms, seemed similar to the use of terminology to describe the various references to ownership interests in the legislation.

Despite the varied terminology used in relation to the law of groups both in the 1990 Law on Enterprises and in Soviet legislation generally, the 1990 Law on Enterprises did however use a particular new legal term that *did* have a broadly accepted meaning. Article 7(1) referred to the right of an enterprise "to create a subsidiaries (*"dochernie predreiyatiya"*) with the right of a juridical person". This was very significant as the term "subsidiary" had been entirely absent from mainstream Soviet law as the concept was not directly relevant to a law on groups developed upon administrative rather than ownership relationships. This one reference to "subsidiary" hinted at the possibility of a change in the nature of the way the law on groups was to be conceived and expressly permitted a relationship between juridical persons based on the ownership of ownership interests of one by the other. A more developed understanding awaited a clearer elaboration of the nature of ownership interest and its significance in the analysis and classification of the juridical person.

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<sup>967</sup> 1990 Law on Enterprises articles 3(1), 7(1), 20(1). These were not terms of art with any precise meaning under Soviet law. One of the few attempts to distinguish the "concern" (*"Kontsern"*), "consortium" (*"konsortsiy"*) and "economic association" (*"khozyaistvennaya assotsiatsiya"*) was the Kirgiz collection of laws entitled *Sbornik Zakonodatel'nykh Aktov i Metodicheskikh Rekomendatsii dlya Predprinimatelei*, 1 ((Mirmeks:1992), pp.298-330) which included a model charter for each type. Although written after the *perestroika* legislation, these terms were products of the Soviet era legislation.



#### 7.5.4.3 Property Responsibility

The provisions of the 1990 Law on Enterprises relating to liability were always going to be "transitional". The 1990 Ownership Law and 1990 Law on Enterprises presented a regime that lacked sufficient clarity as to the nature of the ownership interest of an enterprise, as to the difference between ownership *of* and ownership *by* the enterprise, and as to the relationship between an association and its constituent enterprises. In such circumstances, the provisions relating the respective liabilities of the owners and the enterprise would necessarily be vague. In addition, if the 1990 Law on Enterprises was to be a broad constitution for all industrial juridical persons, one would expect that the rules relating to liability would be contained in subordinate legislation on each specific juridical person.

The corporate law model provides for a "veil" between the owners and the enterprise and hence generally for limited liability of the owners in the context of an insolvency of the enterprise. The alternative concept of "independent property responsibility" was outlined in Section 3.3. A shift to "limited liability" for certain juridical persons would have been expected to have resulted from any move to an economy based on profit.

The 1990 Law on Enterprises introduced a new term, "full property responsibility", to describe the nature of the responsibility of enterprises.<sup>968</sup> It was unclear what the use of the word "full property" ("*polnaya imushchestvennaya*") added. The 1990 Ownership Law provided generally that an owner shall not be responsible for the obligations of a juridical person "created by him" but that exceptions could be established by legislation.<sup>969</sup>

Full property responsibility should be understood as the culmination of the development of the concept of "full responsibility" in the first expression of the participation model,<sup>970</sup> and the development of self-financing and recourse to all assets as in the contract-based concession model and the second expression of the participation model.<sup>971</sup> The move to full property responsibility can probably be regarded as a move towards the possibility of limited liability, and elements of the new economy as described in Section 7.5.5 below supported this view.

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<sup>968</sup> 1990 Law on Enterprises, article 34(1). Full property responsibility was the basic position, although certain additional responsibilities were included for specific situations in particular relating to the use of natural resources and dealings with consumers (article 34).

<sup>969</sup> 1990 Ownership Law, article 5(1). The use of the term "created by him" was unfortunate, because this rule was intended to cover not just owner-founders of juridical persons but also subsequent owners.

<sup>970</sup> Supra Section 6.3.4.3.

<sup>971</sup> Supra Section 5.3.2 and 6.4.1.



However within the continued socialist framework, the interventionist role of the state in particular hindered the introduction of a liability regime understood primarily in terms of the insolvency situation. This was evidenced by the fact that although the 1990 Ownership Law contemplated a regime of limited responsibility, it also contemplated the creation of exceptions, and such exceptions were also included in the law.<sup>972</sup>

#### 7.5.5 *The New Economy and the Role of the State*

The 1990 Ownership Law and the 1990 Law on Enterprises consolidated the previous steps taken during the *perestroika* period by setting out the basic legal principles upon which the new economy was to be based. The preamble to the 1990 Law on Enterprises used the phrase "the development of goods-money relations and a regulated market".

The concept of "goods-money relations" and "a regulated market" evidenced a retreat by the state from its monopoly position as owner of the means of production and from its paternalistic role as subsidiser of enterprises that had been subject to the state plan. The 1990 Law on Enterprises emphasised self-sufficiency and referred explicitly to "profit" to be used both in incentivising effective production as well as in measuring "efficiency". The implicit assumption was that in the absence of profit, an enterprise should be considered for liquidation.

From an economic perspective this was a radical shift in the nature of macro-economic management. However from a legal perspective, it has been argued that both the 1990 Ownership Law and the 1990 Law on Enterprises provided for this new economy to be structured upon, and regulated by, traditionally Soviet legal understandings and theory. For this reason the new framework of the 1990 Law on Enterprises conceived of the enterprises, not in terms of the market economy "general corporation", but as a vehicle both in terminology and function tied to the confirmation model. It was therefore no surprise that the state retained the right under the 1990 Law on Enterprises to control the activities of the enterprise by a mixture of purely legal and "traditionally Soviet" techniques.

The 1990 Law on Enterprises contained provisions where the state had the right to control the activities of the enterprises; and where the state had the right to demand information about the enterprises' activities in order to ensure compliance with legislation. The law also explicitly left open the possibility of further rights of the state in discrete areas.

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<sup>972</sup> See, for example, 1990 Ownership Law, article 26(3): if a state organisation on the budget had insufficient assets to cover claims of creditors, responsibility was borne by the owner.



The law contemplated the right of state agencies and officials "to give instructions" in accordance with competences set out in the legislation. The word "instruction" ("*ukazaniya*") was associated with the language of administrative control and planning; and it was unclear the extent to which the state was intending to reserve the right to give such instructions to enterprises that were not wholly-owned by the state in order to preserve its former role as economic sovereign. In addition to the right to give instructions, the law seemed implicitly to give the state in certain circumstances the right of "interference in the economic and other activities of an enterprise".<sup>973</sup> This was defined negatively - the law stated merely that the state could not interfere in the activities of an enterprise *if* such activities did "not affect the rights of State agencies with regard to carrying out supervision over the activities of enterprises".

Tax and state agencies were given the right to demand information from the enterprise to the extent that they had the right to carry out "control" or "verification" over individual aspects of the activities of the enterprise; including its keeping of accounts in accordance with legislative requirements; its disclosure of commercial secrets capable of harming society; and its payment of tax.<sup>974</sup> This clearly opened up the possibility for significant information gathering exercises and specifically contemplated the existence of state agencies appointed to the task of monitoring these activities.

The law included other provisions that also alluded to the further possibility of state intervention through subordinate legislation. In the area of property, article 10 provided that the enterprise had the right to sell and transfer property, "unless otherwise provided by legislative acts of the USSR and the union and autonomous republics". In the area of profit, article 21 provided that while the enterprise had the right to determine the orientation of the use of net profit, "state influence on the choice of orientations...shall be effectuated through taxes, tax privileges, *as well as economic sanctions*" [emphasis added]. In the area of planning, article 23 provided that while the enterprise had the right to plan independently its activities, "the enterprise shall fulfil work and deliveries for state needs on a contractual basis" and must take into account "ecological, social, demographic and other consequences affecting the interests of the populace on the territory". In the area of economic activities, article 24 provided that while the enterprise had the right to carry out all activities that were not prohibited, it expressly noted that "a list of types of products, work and services the free realisation of which is prohibited or limited shall be established by legislation of the USSR" providing further that "the interests and rights of the consumer shall be protected by

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<sup>973</sup> 1990 Law on Enterprises, article 30.

<sup>974</sup> 1990 Law on Enterprises, articles 32(2), 33(2) and 35(2).



legislation". This principle was expanded in article 31(1) that additionally provided that the state should "ensure the social protection of all working people" when regulating the activities of enterprises. In the area of prices, article 26 provided that while the enterprise had the right to establish prices independently or on a contractual basis, "state regulation of prices shall be permitted for...resources which determine the scale of prices for the economy and the social protection for citizens". Finally, article 34(2) gave the state the possibility to suspend the activities of an enterprise for violations of "the regime of nature use".

The practice of expressing the rights of the enterprise and then tempering their exercise by the use of provisos or by alluding to the possibility of state intervention was not an uncommon practice in the style of Soviet drafting. Indeed article 30(1)) only provided state guarantees for the "rights and *legal* interests" [emphasis added] of an enterprise, suggesting that the Soviet notion of contingent rights and "legitimate" interests may still have been retained. What this meant was that the true "independence" of the enterprise from the state would be ultimately determined by the extent to which the state in practice exploited the wide possibility in the drafting for intervention.

#### 7.5.6 *Creation and Liquidation of Enterprises*

The existence of non-state owned juridical persons did not necessarily entail the introduction of a permissive regime with regard to their creation. As has been illustrated in the previous models, the state had adopted broadly a concession approach in the case of foreign investors and an authorisation regime in the case of the second expression of the participation enterprises.

The general rules relating to the creation of enterprises were set out in Section II of the 1990 Law on Enterprises and initially evidenced a move towards a permissive regime, although again this was tempered by provisos whereby the state retained the possibility for intervention. The creation of an enterprise, subject to the details of any subordinate legislation, was permitted by decision of the founder through the filing of the relevant documents, including the charter, with the competent state body and informing the Ministry of Finance. Registration was required to be made within 30 days.

This seemingly permissive regime then contained a number of further elements which gave the state the possible right to intervene and hence meant that the process for creating enterprises fell short of the right to incorporate which is a prerequisite for characterising an enterprise as a corporate body.



Although the refusal to register an application "for reasons of inadvisability" was prohibited, registration was permitted to be refused "for reasons of violating the procedure for the creation of an enterprise established by legislative acts...as well as the failure of the constitutive acts (or documents) to conform to the requirements of legislation". In addition to this procedure, the law provided for further authorisations and procedures to be followed with respect to the use of a land plot or natural resources (article 5(4) and 11) and for licences to be obtained for certain specific activities (article 8).

The liquidation of an enterprise was permitted by decision of the owner or by decision of a court or arbitration tribunal on the grounds of bankruptcy, failure to fulfil legislative requirements and other grounds specified.<sup>975</sup> Thus in a similar way to the creation regime, the liquidation regime was also sufficiently flexible to enable the possibility of state intervention. The regulation of the liquidation of an enterprise under the 1990 Law on Enterprises was however one of the few areas where the law reflected the new underlying economic realities of the market economy and the importance of profit. This was developed through the provisions relating to the liquidation procedure which included rudimentary drafting to take into account the concept of external creditors and a waterfall of payment rights upon a winding-up.

## **7.6 Whither the General Corporation...**

From a doctrinal perspective, the consolidating legislation of mid-1990 provided the most crucial elements of the legal regulation of industrial organisations in the Soviet legal system during the *perestroika* era. The possibility for the introduction of the general corporate form was a real one. Following the path laid by the contract-based concession and participation models, only a few additional steps needed to be taken. The most important step was the reconceptualisation of the prevailing law on ownership and the replacement of the socialist concept of "forms of ownership" based on the identity principle. A new doctrinal regime needed to be developed on the basis of the generic owner and distinguishing ownership rights on the basis of the property in question and not on the basis of the identity of the owner. A new generic juridical person could have been built upon this new framework conceived of as a subject of civil law with the right to own property issuing ownership interests that were the objects of the right of ownership. Juridical persons would then be classified by reference to their individual peculiarities, including the nature of the ownership interest issued by them, rather than by reference to the changing identity of their owners. Other steps would have followed from this foundation, including a developed notion of equity capital, the right to

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<sup>975</sup> 1990 Law on Enterprises, articles 27(6) and 37(2).



"incorporate" based on a registration regime and a law of groups based on ownership interests rather than administrative mechanisms. Under this *novostroika*, the uniquely Soviet ownership regime of the socialist state enterprise and the creation of a different type of juridical person for each different identity of owner (including one for foreign persons) would have disappeared. Any person would be given the right to own in whole or part any domestic juridical person and would have had the right to control its activities through the legal mechanisms peculiar to its governance regime. Stand alone legislation could have been used to provide additional rules, advantages and procedures governing foreign investment.

The 1990 reforms did indeed have a radical element to them as they evidenced the development of a regulated market based on profit and the erosion of the unitary state. As has been showed, the 1990 Ownership Law not only confirmed the retreat of the state from its monopoly ownership of the means of production but also introduced certain new principles into the regime of civil law and juridical persons, namely the principle of equivalence, the permissive regime, and the rule of law. Each of these principles was further enunciated in the 1990 Law on Enterprises.<sup>976</sup> In particular, despite the fact that the state retained under that law a wide possibility for intervention, the law generally went on to provide for the right of suit against the state should any agency exceed its competence.<sup>977</sup>

However, as has been argued, although the economic realities had moved radically towards embracing the market, the new legal constitution as set out in the 1990 reforms held back and instead retained an underlying structure that was indebted to socialist understandings. The generic owner was deconstructed and undermined by the regime of "forms of ownership" based on the identity principle. While during this time the economic reforms openly leapt towards the market model, the new legal framework for the industrial organisation actually retreated back to the confirmation regime. The generic industrial enterprise of 1990 looked more like an enterprise of the confirmation model than any juridical person that had been introduced since 1987.

The development of the market economy required a generic owner concept, required a developed understanding of the ownership interest of the juridical person, required the

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<sup>976</sup> On the principle of equivalence, the 1990 Law on Enterprises was predicated upon regulating the generic enterprise "irrespective of the form of ownership", a principle noted in various places (see preamble, articles 1(1), 4(1) and 31(1)). On the principle of the permissive regime, the 1990 Law on Enterprises explicitly provided that "an enterprise may engage in individual types of economic activity if they are not prohibited by legislative acts" (article 1(3) and was noted in the context of many other provisions (see articles 2(4), 9(2), 10(3), 18(1), (2), (4) and 24(1)).

<sup>977</sup> On the right to take action against state agencies exceeding their competences, see articles 5(4), 6(3), 13, 30(1), (2) and 32(2).



introduction of equity capital and a juridical person perceived as a vehicle in the first instance for the elaboration of the interests of its owners, without a wider social role. There was no doubt that the economic base would prevail, but the expression of the aspirations of that economy would be forced to operate within a constitution uniquely unsuited to its demands and as such would lead to a law on enterprises that was confused, lacking in clarity and devoid of a coherent and sound footing which fundamentally distorted and misunderstood the nature of the juridical person and its place within the civil law system.

The choice of *perestroika* rather than *novostroika* was fundamental in the development of the law of juridical persons and the ownership regime, not just for the Soviet Union, but for the subsequent regimes of its republics after becoming independent states at the end of 1991. For despite the fact that numerous legislation, waves of reforms and entire new codes have been enacted over the 10 year period since 1991, the basic law on ownership (including in the Russian Federation) continues to be structured upon the logic of the socialist forms of ownership regime based on the identity principle. And so the legacy of the new economic constitution of Spring 1990 seems to have endured, and with it the latent questions and problems for the regulation of a market economy and in particular the law of the industrial organisation.



## 8. CONCLUSIONS

*"Even so, we should speak not of darkness  
but of a somewhat blurred light"*

Michel Foucault

The specific "conclusions" of this thesis have already been set out in the "Short Thesis" introduction. In summary, this study presents a "history" of the foundation of the law on industrial organisations covering the period from 1985 to spring 1990 and thereby offers a teleological doctrinal explanation and understanding of the 1990 economic constitution that formalised the demise of the Stalin command economy. While there are a number of theoretical strands that comprise "the thesis", looking back on the study as a whole, it seems that the central arguments are predicated upon three core "conclusions". I do not believe that any of these conclusions have been advanced before in the literature of this area, either in Russia or outside, and as such, I acknowledge they remain controversial. I hope however that although each is implicit throughout this work, they "emerge from within" both as logically argued and broadly coherent:

The first is the significance of "other branches" of law in the theoretical history of the development of the industrial organisation from 1985. These include the law of collective farms, the law of contract (in particular the contract for joint activity and lease contract) and foreign relations law (in particular the law on joint enterprises).

The second is the importance of Spring 1990 as the point at which the "foundation" of the new law on industrial organisations was finally constituted, framed by a new constitution for the economy and its actors, and promulgated pursuant to the 1990 Ownership Law and 1990 Law on Enterprises.

The third is that both traditional Soviet law, as well as the new economic constitution of 1990, did not contain a developed understanding of the concept of the ownership of a juridical person or "the nature of the ownership interest". Through the retention of the construct of the "forms of ownership", a socialist underlying doctrinal orientation to the law on industrial organisations was ensured; and the law remained insufficient to regulate precisely and comprehensively the new industrial organisations with fragmented ownership and equity investment. For this reason, their characterisation in Soviet law as "enterprises", rather than "companies", accurately reflected their juridical status.



My initial intention was to write a theoretical explanation of the genesis, history and foundation of juridical persons for the period from the early days of *perestroika* to *circa* 1995 (the time when the former USSR republics began to enact new civil codes that consolidated the piecemeal legislation adopted to date). I wanted to encompass not just all-union legislation but also the legislation of each of the former republics for that period. I was already familiar with much of the relevant provisions of Soviet law, as well as the Russian and Kazakh law of this period. My research first took me to each of the Central Asian republics, and starting in June 1994, I spent several weeks at each of the Ministries of Justice in Kazakhstan, Tajikistan, Kirgizstan, Uzbekistan and Turkmenistan. I then visited the Ministry of Justice in Belorussia and was intending next to go to the Ukraine. From each trip I returned with many books and binders of legislation and photocopies of all laws and subordinate legislation directly and indirectly related to the law of juridical persons for the period from 1985 to the date of my particular visit. Much of this material had been classified as "for internal use only", "not for copying" or "secret".

As I developed my understanding of the law of juridical persons, I began to realise how much of its origins lay in the politics and law of the 1920s and 1930s. At that time my knowledge of the early part of Soviet history generally was rather sketchy. And so my research then took me briefly back to the law and history of the NEP era and the first five-year plan. As I immersed myself in the political history of the early years of Soviet power, I began to appreciate the fundamental distinction that was drawn by the Tsarist regime, and by Lenin and his successors, between the "proletariat" and the "peasant", and more generally between "industry" and "agriculture". I began to see how this distinction came to be expressed even through to the Soviet law of the early 1980s that classified civil law and the legal status of state enterprises as entirely separate from collective farm law and collective farms. I still have yet to come across an example of a legal textbook that considered, or considers, industrial organisations and agricultural organisations under the same section or the same cover.

Further research on civil law and collective farm law of the later Soviet period followed. As the scope of my research became broader, my understanding of this area of law became deeper and more precise. First, I concluded that this study should be restricted to the law on *industrial* organisations; but secondly I realised that in order to understand their development I would need to draw upon influences from outside the narrow "law on industrial domestic organisations" as constituted by traditional Soviet law which drew sharp formal distinctions between juridical persons and contract, between civil law and foreign relations law, and between industry and agriculture. I began by considering the simple partnership of the 1922 RSFSR Civil Code which was the Soviet successor to the pre-revolutionary artel and was the



foundation for the contract for joint activity which I then analysed in a new light. I began to understand the place of the 1987 joint enterprises as creatures of domestic civil law. And most surprisingly (to me) I began to see parallels between the collective farm law of the 1930s and the 1987 State Enterprise Law, as well as (perhaps less surprisingly) the 1988 Cooperatives Law.

Having defined the boundaries and scope of this study in terms of "branches of law", I then turned my attention to the periodisation. I had already amassed vast rooms of legislation and secondary materials on all-union and union republic law before it became self-evident that a study encompassing the law of all of the republics would go well beyond the confines of a single thesis. I then knew that much of this research would never appear directly in this study, however it would not have been possible to have defined the limits of this study, and indeed write a meaningful history to a particular point, without a broad understanding of what came afterwards. I decided to begin to write the outlines of the first few Chapters hoping to be led to wherever the logic of the models took me. I was familiar with "theories" of periodisation and had over the course of my research encountered a number of attempts at periodisation in the secondary literature both of the Soviet period generally and also of the Gorbachev years specifically. These have been noted in the footnotes and the body of the preceding Chapters, as appropriate. I knew how easy it was to be seduced into writing history by reference to "landmark" political events and the allure of ending this study with the demise of the Soviet Union in December 1991 was great. I wanted however to devise a periodisation from within the logic of the subject matter of the thesis, by reference primarily to endogenous criteria. In this regard, I found Eric Hobsbawm's refusal to be led by the "obvious" periodisation in his histories of the "long nineteenth century" (1789-1914) and the "short twentieth century" (1914-1991) particularly liberating. Eventually I was driven by three considerations: economic, political and legal.

Gorbachev in his "Memoirs" noted 1990 as the date for the commencement of the final stage of *perestroika*, and it is broadly accepted that 1990 marked the start of the most radical phase of economic reforms aimed at introducing market mechanisms into the Soviet economy. This was evidenced by the debates over the 1990 budget and the publication of various competing economic plans and programmes prescribing the necessary steps and stages along the path ahead.

At a political level, in the aftermath of the revolutions in Eastern Europe of the previous year, 1990 saw the independence movements within the Soviet Union itself become more acute. Soviet tanks were mobilised after the Lithuanian parliament on 11 March voted almost



unanimously for the restoration of its independence. Lithuania seemed to symbolise the nationalist tensions throughout the USSR, and between August and October, 10 of the 16 autonomous republics of the RSFSR declared their sovereignty. 1990 was the year when a new political settlement of the USSR moved from being a question of "if" to a question of "when", and the first draft of a new treaty was presented for public discussion by Gorbachev on 23 November.

Both the economic and the political were reflected in the legal framework of 1990. Up until 1990 *perestroika* had developed almost exclusively through all-union legislation. In the area of industrial organisations, various pieces of legislation had been adopted that introduced in an apparently *ad hoc* way a series of "new" juridical persons. In 1990 two generic pieces of legislation were enacted at the all-union level: the 1990 Ownership Law and 1990 Law on Enterprises. As has been argued, I gradually came to see these two laws as "new constitutions" for the Soviet economy and moreover as the culminating legislation of the "founding stage" of the new law on industrial organisations. After spring 1990 the economic, political and legal forces fragmented the "centre" of the Soviet state, relocating it among the republics. Different economic plans for different republics were devised, different political aspirations were aired and different legislation was adopted. In late 1990 "the war of laws" commenced and the republics began to ignore the restraints of all-union law and adopted legislation on the basis of their "own" politics. The law of juridical persons of the different republics dates not to their formal independence in December 1991 but to their actual independence seized during the months of late 1990. Thus, for example, when the RSFSR became a new independent state (the Russian Federation) at the end of 1991, that state had already adopted its own constitution (which had been amended several times since 1990), and its own land code, and laws on ownership, privatisation, enterprises and entrepreneurial activity, competition, investment activity, foreign investments, and a statute on joint stock societies - all were enactments passed during the period between 1990 and 1991. This republic legislation of 1990-1991 was not based on the restrictions in the prevailing all-union legislation of that time, but instead proceeded from and was constructed upon the foundations forged by the all-union legislation of the previous *perestroika* reforms of the period from 1985 to 1990. The all-union 1990 March Constitutional Amendments, 1990 Ownership Law and 1990 Law on Enterprises were the final consolidating framework marking the *de facto* end of the supremacy of all-union legislation. It therefore seemed appropriate to end at that point a study based on all-union law and focused on the *foundations* of the new law on industrial organisations.



Having decided upon this particular scope and periodisation, I then realised that the thesis would inevitably present an entirely new history of the subject. However, what I regard as the most novel and critical element of that history developed later and rather unexpectedly. I had always sought to conceptualise and practise Soviet law "from within the assumptions of that system". This I saw as a strength, for it is always the challenge of the comparativist to enter into the mindset of his subject. However in the development of the models presented in this study and in the construction of the general framework, I was determined also to think outside the systemic constraints of Soviet law by reference to abstract theory as opposed to within the logic of the text. As the models evolved, so my thinking took me to unexpected places. I assumed however that I had reached the limits of my analysis through the incorporation of the law of contract, foreign relations law and collective farm law. However in the elaboration of each model I was continually taken back to the law on ownership. I had always been uneasy about the doctrine of "forms of ownership" in a market economy context but was never sure why. I was familiar with the various debates *in academe* about the nature of the ownership interest of the post-Soviet juridical persons but had never generalised or abstracted beyond the specifics of those debates.

The writing of my thesis was very far developed before I finally understood with clarity the principal shortcoming of the Soviet law on ownership. I believe my myopia was due in part to the skill of Venediktov and others in constructing a "coherent" law on ownership for a command economy without the necessity of tackling what was in all other economic systems a keystone concept in this area of law, namely the question of the ownership "of" a juridical person and the nature of "the ownership interest".

Once identified, I began to re-read much of the source material that I had already read so many times previously in an attempt to identify any clues as to the legal nature of the state's ownership interest of a state enterprise, and as to who, if anyone, "owned" a collective farm. Neither of these questions were posed anywhere in that material, nor in any other works that I had encountered. There seemed to be an almost hypnotic silence - an absence so obvious that it was constantly overlooked. As I played with this idea, I came to realise that it was the mask of the regime of "forms of ownership" that obscured the identification of the absence of this concept. Looking back upon the Chapters I had already written, I saw that the law during the late 1980s eroded one-by-one the tenets of the confirmation model, but that the forms of ownership regime based on the identity principle always remained, and with it an incomplete understanding of the significance and nature of the ownership interest of the juridical person.



My thesis was largely re-written. When reaching the final Chapter on the 1990 reforms, I came to see the tension latent in the drafting of the new constitution of 1990 - a tension between the generic owner and the "forms of ownership regime". I then understood that the year 1990 had presented the possibility for *novostroika*, and that legislators had recoiled, opting instead for a framework that "acknowledged" a new economy but that was rooted in traditional socialist understandings. With an eye on the period after 1990, it was apparent that the retention of this socialist framework was in part responsible for the "strange" classification of juridical persons; was in part "responsible" for the bifurcation in the law of juridical persons between "foreign investment juridical persons" and "domestic juridical persons" (embodied in the subsequent legislation on foreign investment); and most importantly was in part responsible for retarding a comprehensive and coherent analysis of the nature of the ownership interests of different juridical persons, and ultimately of the juridical person itself. The drafting of future legislation in this area was strained and contorted due to the mismatch between the practical demands of a market economy and the socialist doctrinal principles underlying the positive law framework of the "new" law on ownership.

All studies and all histories must of course be limited by scope, periodisation and content. And in the context of this study, they have been carefully chosen, constructed and argued in an attempt to put forward certain alternative understandings. It is only hoped, when the history of the law on industrial organisations of the former republics *after* 1990 is eventually written, or when lawyers struggle to make sense of current legislation in the former republics, that in some small way, the insights, ideas and theories offered by this study can be of help in shining a light and casting shadows where previously there may have been darkness.

**Stephen Lucas - April 2002**



## APPENDIX I

### Abbreviations

The following abbreviations are used in this study:

#### 1. Constitutions, Fundamental Principles and Codes

1918 RSFSR Constitution:	Konstitutsiya (Osnovnoi Zakon) RSFSR (1918).
1922 RSFSR CrimC:	Ugolovnyii Kodeks RSFSR (1922).
1922 RSFSR Civil Code:	Grazhdanskii Kodeks RSFSR (1922).
1922 RSFSR Land Code:	Zemel'nyi Kodeks RSFSR (1922).
1924 USSR Constitution:	Osnovnoi Zakon (Konstitutsya) SSSR (1924).
1924 FPCrimL:	Osnovnykh Nachal Ugolovnogo Zakonodatel'stvo Soyuza SSR i Soyuznikiy Respublik (1924).
Stalin Constitution:	Konstitutsiya (Osnovnoi Zakon) SSSR (1936).
1960 RSFSR CrimC:	Ugolovnyii Kodeks RSFSR (1960).
1961 FPCivL:	Osnovi Grazhdanskogo Zakonodatel'stvo Soyuza SSR i Soyuznikh Respublik (1961).
Kaz CC:	Grazhdanskii Kodeks Kazakhskoi SSR (1964).
RSFSR CC:	Grazhdanskii Kodeks RSFSR (1964).
Kaz CCP:	Grazhdanskii Protsessial'nyi Kodeks Kazakhskoi SSR (1964).
RSFSR CCP:	Grazhdanskii Protsessial'nyi Kodeks RSFSR (1964).
1968 FPLand:	Osnovy Zemel'nogo Zakonodatel'stvo Soyuza SSR i Soyuznikh Respublik (1968).
Brezhnev Constitution:	Konstitutsiya (Osnovnoi Zakon) SSSR (1977).
FPLease:	Osnovy Zakonodatel'stvo Soyuza SSR i Soyuznikh Respublik ob Arende (1989).
1990 FPLand:	Osnovy Zakonodatel'stvo Soyuza SSR i Soyuznikh Respublik o Zemle (1990).
1990 FPIInvA:	Osnovy Investitsionii Deyatel'nosti v SSSR (1990).
1991 FPCivL:	Osnovy Grazhdanskogo Zakonodatel'stva SSSR i Respublik (1991).
1991 FPForInv:	Osnovy Innostranii Investitsii v SSSR (1991).
1994 RSFSR CC:	Grazhdanskii Kodeks Rossiiskoi Federatsii (Chast' Pervaya, 1994; Chast' Vtoraya, 1996).

#### 2. Laws

State Enterprise Law:	O Gosudarstvennom Predpriyatii (Ob'edinenii) (1987).
Cooperatives Law:	O Kooperatsii v SSSR (1988).
1990 Law on Enterprises:	O Predpriyatiyakh v SSSR (1990).
1990 Ownership Law:	O Sobstvennosti v SSSR (1990).



### 3. Dekrets, Decrees, Statutes and Edicts

1923 Trusts Dekret:	Dekret o Gosudarstvennykh Promyshlennyykh Predpriyatiyakh, Deistvuyushchikh no Nachalakh Kommercheskogo Rascheta (Trestakh) (1923).
1927 Trusts Dekret:	Polozhenie Gosudarstvennykh Promyshlennyykh Trestakh (1927).
1927 Joint-Stock Societies Statute:	Polozhenie ob Aktsionernyykh Obshchestvakh (1927).
1935 Artel Charter:	Primernye Ustav Sel'skokhozyaistvennoi Arteli (1935).
Enterprise Statute:	Polozhenie o Sotsialisticheskom Gosudarstvennom Proizvodstvennom Predpriyatii (1965).
1969 Collective Farm Charter:	Primernyi Ustav Kolkhoza (1969)
Industrial Association Statute:	Obshchego Polozheniya o Vsesoyuznom i Respublikanskom Promyshlennyykh Ob''edineniyakh (1973).
Production Association Statute:	Polozheniya o Proizvodstvennom Ob''edinenii (Kombinate) (1974).
Decree 48:	O Poryadke Sozdaniya na Territorii SSSR i Deyatel'nosti Sovmestnykh Predpriyatii, Mezhdunarodnykh Ob''edinenii i Organizatsii SSSR i Drugikh Stran - Chlenov SEV (1987).
Decree 49:	O Poryadke Sozdaniya na Territorii SSSR i Deyatel'nosti Sovmestnykh Predpriyatii s Uchastiem Sovetskikh Organizatsii i Firm Kapitalisticheskikh i Razvivayushchikhsya Stran (1987).
Lease Decree:	Ob Arende i Arendykh Otnosheniyakh v SSSR (1989).
1990 October Edict:	Ukaz Prezidenta SSSR, Ob Inostrannykh Investitsiyakh v SSSR (1990).

### 4. Journals; Collected Works and Legislation

IRS:	M.S.Gorbachev, Izbrannye Rechi i Stat'i.
Lenin:	V.I.Lenin, Polnoe Sobranie Sochinenii, Izdanie Pyatoe.
Postanovleniya:	Postanovleniya Soveta Ministrov SSSR - dlya sluzhevnogo pol'zovaniya.
SDZ:	Sistematicheskoe Sobranie Deistviyushchikh Zakonov (c.1973-).
SgiP:	Sovetskoe Gosudarstvo i Pravo
SP:	Sobranie Postanovlenii Pravitel'stva.
Stalin:	I.V.Stalin, Sochineniya.
SU:	Sobranie Uzakoneniii i Rasporiazhenii RSFSR.
SZ:	Sobranie Zakonov i Rasporiazhenii SSSR.
Vedomosti:	Vedomosti Verkhovnogo Soveta.
Vedomosti SND:	Vedomosti Soveta Narodnykh Deputatov i Verkhovnogo Soveta.



## APPENDIX II

### Citations and Bibliography

#### A. CITATIONS

Any citation set out in full in the first place that it appears in the footnotes. Subsequently, citations are made by referring back to that first footnote where it appeared in full. Where there is more than one full citation in the first footnote, a date is used to indicated the relevant cite.

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